THE POST-WAR UNEMPLOYMENT PROBLEM

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THE POST-WAR UNEMPLOYMENT PROBLEM

BY

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"Sir, you must not neglect doing a thing immediately good, from fear of remote evil."
DR. JOHNSON.

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TO

W. W. S.

WHO OUGHT TO HAVE WRITTEN THIS BOOK HIMSELF INSTEAD OF AIDING AND ABETTING THE AUTHOR

PREFACE

Most of the material and much of the work embodied in the following pages had been done before unemployment became an issue in a General Election. My first impulse was to go no further with it. As the controversy developed, however, it seemed to me that the parties were at cross-purposes; that the Liberal and Labour thesis, that additional employment could be provided at once by capital expenditure on public works, was quite consistent with the Conservative thesis, that unemployment could be permanently relieved only by bringing down costs. It seemed to me also that interest in the problem might survive the election, since voting by itself would not solve it, and that there might be a use for a summary and analysis of the more important factors in it. So far as I have any aim beyond offering this, it is to discourage the hope that the problem, if left to itself, will cure itself, and to argue that the necessary reorganisation of the depressed industries will not be effected unless the initiative is taken and the impulse given by some agency outside them.

These conclusions are contained in the last chapter. I have prefaced them with a summary of the rest of the book, for the convenience of readers who are more interested in conclusions than in the processes by

which they are reached. I am indebted to Miss Sybil Simpson for assistance in preparing the tables and diagrams in the book, and to my wife and Miss Simpson for seeing the book through the press in my absence abroad.

HENRY CLAY.

MANCHESTER
June 4th 1929.

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CHAPTER I

UNEMPLOYMENT: PRE-WAR AND POST-WAR

I. *Pre-War Unemployment*

Unemployment is not a new problem. In the decade before the war it was the object of intensive study both by private investigation and by the Royal Commission on the Poor Laws, which reported in 1909. It is necessary to summarise the results of this pre-war study, in order to discover, by comparison and contrast, the elements in the problem that are peculiar to post-war conditions. A large part of the difficulty of dealing with post-war unemployment is to know how far it is due to permanent influences, inherent in industry, of which we were beginning to have some understanding, how far it is due to temporary and abnormal causes connected with the war.

In the first place, it was made clear that unemployment was "a problem of industry", not a problem of personal defect.[1] It arose from fluctuations in the volume of employment, which occurred irrespective of the economic quality of the available workers. Personal defect might determine on which, of a number of workers, unemployment at any time should fall, when unemployment was inevitable for some; but that some

[1] W. H. Beveridge, *Unemployment: A Problem of Industry*, 1909.

unemployment was inevitable was due to general causes inherent in the organisation of industry.

In the second place, unemployment was shown to be a problem of *adjustment*, of the supply of labour to the demand for it. The experience of the seventy years before the war showed no tendency towards an increase in unemployment, in spite of a great increase in population; nor did it point to any decrease, in spite of the creation of many new industries. It was a permanent problem, in the sense that the adjustment was necessary (and difficult), whether population was increasing, declining, or stationary, and whether existing industries were expanding or new industries taking their place. Declining industries might make recovery from a period of unemployment more difficult, and new industries make it easier; but the fluctuations in employment persisted, in new industries as well as in old, without any significant change, so far as could be discovered, in the average proportion, over a decade, of the population in employment.

With this indication of the general character of the problem it is possible to proceed to an analysis of its chief elements.

Even if the volume of industrial activity *as a whole* did not vary, and the relation of the demand for labour to the population seeking work were constant, there would still be unemployment. The nature of the demand for labour and the nature of labour itself both make it inevitable. Thus the *aggregate* demand for labour might not vary, or might increase uniformly in the same ratio as the population of working age; but, being made up of discontinuous and dispersed demands for particular kinds of labour, leave always a part of the population unemployed. A housing scheme

might be completed in one place, and an exactly equivalent demand for labour might be created by the commencement of another housing scheme in another place; but there would still be unemployment, if the new work was inaccessible to the labour displaced by the completion of the first scheme. Or the launch of a ship in one yard might take place at the same time that an equivalent ship was placed on the stocks in another; or the completion of the unloading of a ship in one dock might coincide with the arrival of another ship in another dock ten miles down the river; but the maintenance of a uniform *aggregate* demand for labour would not prevent unemployment. In these cases there is no change in the kind of labour demanded; but constant change is going on. The average level of unemployment before the war was maintained by the growth of new industries to fill the place of declining industries. Some unemployment was probably inevitable in the case of workers specialised to a declining industry, who were too old to learn a new occupation when it ceased to need them. The demand for labour as a whole is normally an aggregate of particular demands for discontinuous, dispersed and changing pieces of work.

Similarly labour is only imperfectly mobile. Where industrial development is not dislocated by war or other catastrophe, the adjustment to changing demands can usually be made by directing the new generation to new work without disturbing the old generation in the old work; but it is not possible to re-direct and re-distribute the industrial population with every change in the demand for labour. The mere distance of new work from the old involves a time-lag in the adjustment of labour-supply to the demand, if

the labour is able to move. But labour is not always able to move; there may be no housing accommodation where the new work is developing; the unemployed worker may be a member of a household the other members of which are in work, as is so frequently the case in textile districts. Or the worker may not be able to adapt himself to the needs of the new work. Quite apart, therefore, from fluctuations in the aggregate volume of employment, there must always be some loss of work, due to the impossibility of fitting workers, whose mobility and range of capacity are limited, to the kinds of work available.

Employment, as a whole, however, does fluctuate, and, while the growth before the war tended to keep pace with the growth of population, there were constant fluctuations about the trend of growth.

It is possible to distinguish several kinds of fluctuation. In certain employments the volume of work varies from day to day. Work at docks, which depends ultimately on the volume of goods to be moved, but is constantly dislocated by wind and tide, affords the chief example of daily fluctuation. The effect on employment depends on the method of engagement. The work offers an opening for a regular staff, capable of handling the minimum of work to which the docks are ever reduced, with a mobile reserve to deal with fluctuations above that minimum. If each taking-on station, as was formerly the practice, acts independently, each will require a reserve of its own, and the industry as a whole will have a reserve in excess of its needs. Moreover, the chance of a job under the system of casual engagements will attract to the industry more than can be employed even at its busiest, with a necessary consequence in chronic under-

employment. Some occupations, again, fluctuate with the seasons, either because their materials come in at certain seasons only, or because the demand for their products is seasonal.

Variations in employment due to these fluctuations, like the time-lag in the fitting of available workers into available jobs, are the less difficult elements in the problem to distinguish. Moreover, to distinguish them is to indicate appropriate remedies; a system of employment exchanges to bring together vacancies and workers and to eliminate unnecessary movement in search of work, some system of vocational guidance for new entrants to industry, the concentration of casual jobs by a system of preference upon the minimum number of workers wanted, and the dovetailing of seasonal jobs. If these elements are not dealt with, it is not for want of knowing how to deal with them, but due to lack of will. The case is different with the fluctuations in the activity of industry, which were the chief causes of pre-war unemployment.

II. *Industrial Fluctuations*

Industrial fluctuations are the subject of an extensive and a growing literature. It would be idle to attempt to summarise this for the purpose of the present inquiry; but something must be said, if we are to contrast the post-war and pre-war employment situations. The nature of them is illustrated by the two diagrams (I. and II.) that follow. The first represents the changes in the percentage of unemployed members of trade unions that paid out-of-work benefit, and the movement of wholesale prices; the figures on which it is based are annual averages, so that the influence of

seasonal and other short-term fluctuations is eliminated; the secular trend of prices—upwards to 1873, then downwards to 1895, and then upwards again—has been eliminated, and the fluctuations about the trend alone given. It may be compared with the similar chart in the Second Fiscal Blue Book, which distinguishes the movement of employment in certain groups of industries, and suggests that, although industries fluctuate to some extent independently and with varying degrees of amplitude, they are all affected by

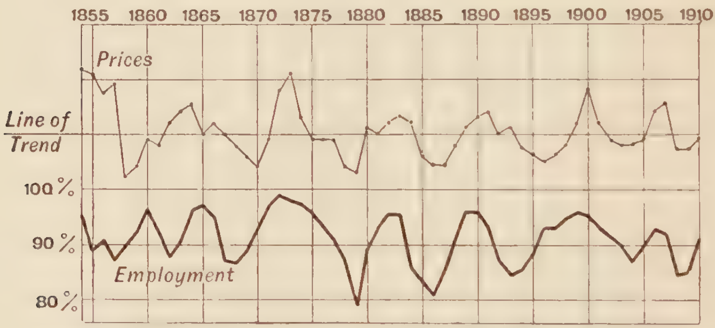

FIG. 1.—FLUCTUATIONS IN PRICES AND EMPLOYMENT, 1854–1910.

some general influences that produce fluctuations in industry as a whole. The second similarly illustrates the fluctuations in wage-rates and prices.

What these general influences are is the chief subject of controversy. Certain conditions of modern industry, however, obviously predispose industry to fluctuation. Industrial production is a lengthy process, necessarily carried on ahead of demand. The final consumer can buy what he wants in a shop by asking for it, only because the shopkeeper, and the wholesaler and manufacturer who supplied him, anticipated his want, and were producing for it months and years

ahead. Production, therefore, is carried on on an estimate of demand; the task of making this estimate is concentrated on pivotal firms that give orders to others, but production as a whole is carried on in anticipation of demand, not in direct response to it. The fluctuations, therefore, which are the normal characteristic of modern industrial activity, represent the errors in anticipation and estimate of the business-men who direct production to demand. At one time they overestimate what the consuming public will

Fig. 2.—Fluctuations about Trend: Wages and Prices, 1855–1908.

take, with the result of over-production; at another they underestimate, with the result of under-production. It must be clearly understood that over-production does not mean production of more than can be consumed, nor even of more than can be sold; but simply production of more than can be sold at the anticipated price, or at some lower price that will still cover all the costs of putting the goods on the market. Thus there appears to be in the nature of modern industry an inherent tendency, at one time to over-estimate demand, with the result that there is over-production, which checks industry and leads to depression; at another to underestimate, with the result that

demand is not satisfied, prices rise, and industry is stimulated.

It is no criticism of the business-man to attribute trade fluctuations to errors in his anticipation of demand; for the difficulties in the way of correct anticipation are insuperable. Some of the chief difficulties may be mentioned. The ultimate source of economic supplies is nature, and natural supplies are not under perfect control. Some irregularity in production must follow from variations in harvests, which will also affect the purchasing power of agricultural populations and so bring in another element of irregularity. The Lancashire cotton industry, dependent on American harvests for its supplies and on the Indian agriculturalist for a large part of its market, is the type of this difficulty. A second, less obvious, difficulty is this. Industries are partners; few, if any, cover the whole space between the natural raw material and the finished article. If production is to be regular and uniform, it is necessary, therefore, that the different co-operant industries keep in step; but this is difficult, because different industries have different productive periods and respond with unequal speeds to an increased demand. The response of industry to an exceptionally large wheat crop in North America has been traced on several occasions. Additional railway transport was needed and additional shipping tonnage, and these could be provided only by an expansion in the engineering, shipbuilding, and iron and steel industries. Thus a temporary, though large, expansion in the volume of wheat to be moved, by its immediate influence on railway receipts and freights, would lead to increased activity in shipbuilding, which resulted in ships being launched long after the occasion that

called for them had passed, in railway extensions that might not pay for years, and in a stimulus to the iron and steel industries, that inevitably tended to be followed by reaction because the originating cause was transient. Intensifying these is the influence of competitive and unco-ordinated production. Conceivably all the firms in an industry might anticipate accurately the *aggregate* demand for the industry's products in a coming season, and yet, because each overestimated his *share* in it, put on the market more than it would take at prices that covered costs.

Errors in anticipating demand, and so in adjusting supply to demand, are probably inevitable. Why do they tend to occur at approximately the same time, and in the same direction, in different industries? The explanation is probably to be found in the mutual dependence of industries on one another and their common dependence upon the credit-agencies of the country. The industries are one another's customers, and anything that affects the prosperity of one industry will affect the prosperity of industries selling to it or to its personnel. Moreover, the effect will be almost simultaneous, because, industry being compelled to anticipate demand, the initiating impulse will be perceived and allowed for at once by business-men in industries in which it exerts only a derived and secondary effect.

If, however, the money and other means of payment, which the community has to pay for products and services, were strictly limited and inexpansible, then expansion in one industry could take place only at the expense of contraction in others. If the country spent more on woollens, owing to a cold winter, it would have less to spend on other things,

and the expansion in the woollen industry would be counter-balanced by contraction somewhere else. Means of payment are, however, not absolutely limited. Even if the possibility of drawing gold from other countries be left out of account (since obviously not all countries can avail themselves of it simultaneously and pre-war fluctuations tended to be international in scope), there is an element of elasticity afforded by credit. Banks can increase the ratio of their deposits to their reserves; in addition, these deposits can be turned over more rapidly. Thus, one industry can expand, drawing to itself a larger amount of means of payment, without drawing from others, and the effect of its increased prosperity will spread, stimulating other industries, and either increasing their output or raising their prices. Banks cannot, however, disregard the ratio of their liabilities to their cash resources. If the latter cannot be increased, it will be necessary at some point to check the expansion of credit, which will in turn check the activity of industry. It will be necessary to refer to the influence of credit again in connection with the next influence that it is necessary to examine.

We have seen that fluctuations are to be expected, since an exact adjustment of production to demand is too difficult a task to be accomplished with complete success every time, and that the common dependence of all industries on the credit-system will tend to make expansion and contraction in different industries more or less simultaneous. It remains to point out that fluctuations once started, however generated, will tend to perpetuate themselves. The course of the fluctuation itself dislocates the harmony of industrial production, distorts the nice adjustment after which business

strives, and compels an alternation of improving and declining trade. Stability for any number of years, uniform activity, or a uniform rate of increase, is the one condition that pre-war industry never exhibited.

Production, we have seen, is controlled by business-men, who are working for profit. If profits expand, an expansion of production may be expected ; if they contract, or change into losses, a contraction of production. Now profits on the whole will expand or contract mainly under the influence of three factors—costs, selling-prices, and volume of output. If selling prices and costs always moved together, so that the producer's margin did not vary, there would still be fluctuations, for the reasons we have already considered, but their amplitude and regularity would be less. In fact, these two sets of prices do not move together. Annual figures, such as were used in the diagrams given above, conceal their divergent movements, which are fundamental to the problem. A closer examination is needed, which will bring out the relations in time of movements of costs, selling-prices and output.

A revival of trade usually begins with an expansion of demand at the pre-existing level of prices. Provided these leave the producer some margin of profit, the increase in turnover increases his profits and provides a stimulus to industry generally. Not all commodities, however, can be supplied in increased quantities without notice, and the prices of those that cannot be increased will tend to rise. Similarly, when productive capacity in general is fully occupied, any further increase in demand must raise prices. In this rise of commodity prices is a further source of increased profits, and therefore of stimulus to increased industrial

activity. Raw material prices tend to rise sympathetically, but other costs cannot be adjusted so rapidly. Wage-rates, as Fig. 2 showed, lag behind commodity prices, fixed interest charges, bank interest, rents, all lag behind, thus leaving a broadening margin of profit on each unit of output.

The time must come when wage-rates and other costs have to be adjusted to the higher level of commodity prices. Labour costs will rise also from the absorption of the less efficient workers into employment and the payment of overtime rates. Existing plant will be strained, and loan capital for extensions will cost more. Bank credit charges will rise as demand for additional accommodation grows. As costs rise, the rise in selling-prices is likely to be checked. It is easy in times of rising prices and trade boom to make profits merely by expanding existing forms of production. The increased output of the *same* commodities must, sooner or later, satiate the public demand for these commodities, and, in the absence of any diversification of production to new purposes, check sales.[1] Thus costs approach selling-prices; a narrowing margin of profit accompanies a check to sales and output.

Once it is perceived that the margin of profit is likely to disappear, a crisis, or at any rate a turn from boom to decline, is certain. Orders will be cancelled or reduced, stocks accumulate until forced realisations bring prices down. The demand for credit to carry stocks, and to support industry when demand is checked, will put a strain on bank reserves and compel credit restriction, which will also tend to bring prices down.

[1] Capital applications in a boom in order to extend the output of an *undiversified* range of products will intensify this "over-production". Observation of its effects has led some writers, notably Mr. J. A. Hobson, to attribute trade fluctuations to "over-saving".

The losses and unemployment resulting will involve a curtailment of demand, and so further unemployment.

As costs lagged in the upward phase of the cycle, they lag after prices in the downward phase. Wage-rates are maintained at levels that do not permit full employment; debenture and other interest charges, incurred when profit-margins were high, remain high now that profits have disappeared. Recovery comes only when the processes that brought the boom are reversed. Labour-costs are brought down, partly by reduction in wage-rates, partly by the discarding of the less efficient margin of workers, partly by an increased output from the workers in employment. Loan charges are reduced by liquidation, or by replacement by loans raised at lower rates of interest. Methods of production are overhauled, while the average efficiency of industry is raised by the elimination through bankruptcy of the weaker firms. Thus costs are got down to a level, which leaves a margin even at the lower selling prices now ruling. Meanwhile consumers, who held off while prices were falling, are forced to come back by exhaustion of stocks, and are tempted by low prices and new varieties of production. Thus the conditions of profitable enterprise are restored, and the upward swing of trade is resumed. Summarising the experience of the generation before the war, Professor Wesley Mitchell, the writer who has done most to elucidate the nature of the business cycle, was able to say: "Prosperity breeds the crisis that leads to depression, and depression produces of itself the conditions that restore prosperity".

This explanation requires supplementing at one point.[1] Whence are the means of payment forthcoming,

[1] Cf. Sir William Beveridge, reviewing *Business Cycles and Unemployment* in the *Economic Journal* of March 1924, p. 94: "The summary de-

that make possible a general rise in prices during a boom, and how are they retired when prices fall in a depression? The answer is to be found in a comparison in point of time between the movements of industrial activity, prices and credit. The statistics available before the war do not enable a very exact comparison to be made. If, however, the trade union unemployment percentage (reversed, to convert it into an index of employment) be taken to represent industrial activity, and the *Statist* index number to represent prices, we find that the fluctuations in employment usually precede price fluctuations by from three to six months. If, then, we compare the prices with credit fluctuations, taking aggregate bank advances (after eliminating a marked secular trend) as representative of the latter, we find that price movements tend to be followed by credit movements with a similar lag of about three months (*cf.* Fig. 3).

Thus the order of movement would appear to be, first, production, then prices, then credit. Now this is the order that we should expect from observation of business. Production increases, because additional orders are placed as soon as the reduction of costs and the revival of demand have made expansion possible at a profit. At this stage prices do not rise, and the business-men, who place the orders, rely for means of payment either on accumulated bank balances or on bank advances which they will apply for later. With reviving confidence and expanding production, buyers begin to offer higher prices. But prices in wholesale trade are seldom cash prices; they are contract prices,

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scription of business cycles (based, of course, mainly on Professor Mitchell's earlier book) leaves rather glaring the gap in his argument as to why prices rise from a depression".

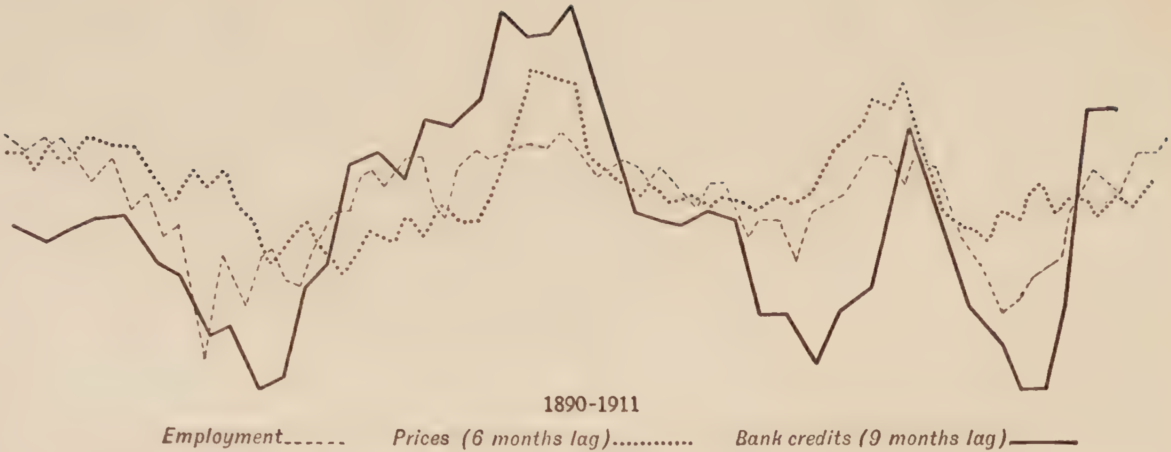

FIG. 3.—RELATIVE MOVEMENTS OF EMPLOYMENT PRICES AND BANK ADVANCES, 1890–1911.

Note.—The curves were plotted separately and then superimposed in such a way that the price figure for September and the bank credit figure for December in each year were on the same point in the time scale as the employment figure for March.

which affect quotations, and therefore price index numbers, some time before it is necessary for the buyers, who have agreed to pay them, to find means of payment. These have to be found, when the contracts are completed and delivery made; then, and not till then, is it necessary to apply to the bank for advances, and even then only if the buyer has no accumulated deposits to draw on. We should expect bank advances, therefore, to be affected after prices, though the rise in prices may have been based on the anticipation that such advances would be forthcoming.

The answer to our question, why do prices rise, and, before that, how can industry expand, is to be found in an increase in the means of payment. When trade begins to improve, additional means of payment are forthcoming in the turnover of idle and dormant deposits. When this increased velocity of circulation of existing means of payment is insufficient, additional means are created by expanding the volume of credit advances on a given cash reserve. If cash reserves are increasing, either because the Government is printing paper money or because gold supplies are being rapidly increased, the expansion of business and the rise in prices can continue without check. Before the war, however, a check was usually inevitable, since cash reserves could not be increased rapidly, and banks would be forced to put up the price of credit, or otherwise restrict it, when the ratio of demand liabilities to cash seemed to them dangerously high. At the crisis advances would be increased, at almost any cost, to carry important customers over the crisis, while deposits would be depleted by the same need; but in the depression deposits would tend to accumulate and lie idle, since firms could not make a profitable use of

their resources, while advances relatively declined, because, even at low rates of interest, if costs could not be covered at current selling prices, businesses would not want bank advances. Idle deposits are the equivalent of locking up so much of the means of payment, and the reduction in bank advances equivalent to the retiring of so much more; so that the fall of prices in the downward phase of the business cycle is amply accounted for.

III. *The Post-War Cycle*

The factors in the pre-war problem of unemployment, that were distinguished in the preceding sections, all persist in the post-war period; but some have had their influence amplified and exaggerated by the war. There is no reason to suppose that the loss of employment involved in the inevitable delays in the fitting of available labour into available jobs is either greater or less than before the war. On the one hand, a national system of employment exchanges, intimately associated with industry by the administration of a national system of unemployment insurance, has probably tended to reduce the time wasted in finding such jobs as are available; on the other hand, a shift in the territorial distribution of industry, which it will be necessary to explain later, has occasioned a greater need of movement, and a general shortage of housing accommodation has obstructed movement. Similarly seasonal unemployment is much what it was, except in so far as the employment exchanges have been able to dovetail seasonal jobs. The under-employment associated with casual engagements persists. Registration schemes have been introduced at twenty-five of the larger ports of Great Britain, but at none of them has

the number of men on the register been limited to the number who can be afforded regular employment. And other influences, particularly the larger surplus of labour seeking jobs, have made for an extension of casual engagements.[1] The country still prefers the admitted evils of casual employment to the drastic remedy of compelling employers to make all such engagements through an Employment Exchange; and the provision of relief by insurance has diverted attention from the evil. On the other hand, the factor of industrial fluctuation has been obviously and extensively affected.

It is not easy to distinguish this effect of the war from its other effects. Yet it is important to make the attempt. Of the influences delaying trade recovery in 1921 and 1922 the uncertainty of the economic future was perhaps the chief. The war had moved familiar landmarks, diverted trade from accustomed channels, introduced new factors into the problem of business forecasting; with the result that the business man could no longer have the confidence in his judgment of business tendencies which is the mainspring of enterprise. Some of the new factors in the problem, in particular the novel and immensely increased influence that Governments had on the course of business, were quite incalculable; among the more purely economic factors the most important were the upward and downward movement of industrial activity, a movement that the war seemed to have exaggerated, and the effect of the war in dislocating or damaging the economic organisation of society. Much of the business man's uncertainty was due to the difficulty of disentangling these two sets of influences: yet they were distinct and needed

[1] Cf. R. C. Davison, *The Unemployed*, pp. 180-181, 207-209.

separate consideration. The former was an effect that may be expected to work itself out in the course of a short cycle of years, the latter would require a generation or more.[1]

The statistical evidence suggests that the war interrupted and prevented a depression that was developing after the prosperity of 1913; but the war years are so abnormal that they cannot be fitted into any regular scheme, and it is only their influence on the post-war boom and slump that we have to consider. This influence is to be seen in at least four important conditions that differentiated the post-war boom from any previous boom.

In the first place, the rise in prices was of quite abnormal steepness, indicating both an abnormal demand for commodities and an abnormal difficulty in expanding production to meet this demand. The abnormal demand was due to the starving of civilian markets during the war; it was a banked-up demand, due to the restriction of consumption during four years of immense business activity. There is no need to stress this influence. The difficulty in meeting the demand was due in turn not only to the conversion of industry to munitions work, but also to the starving or overstraining of fundamental economic services during the war. As a result, the railways were short of rolling-stock, their tracks in need of repair, and their organisation unable to meet a sudden call upon them to handle new traffic in new directions: there was a shortage of shipping, due not so much to the destruction of the war as to the congestion at ports and to the

[1] This and the six following paragraphs are taken from an article contributed to the Reconstruction Supplement of the *Manchester Guardian Commercial* for May 23, 1923.

withdrawal of ships for reconditioning; coal production was low, and cost of production high, as compared with 1913. Similarly, there was a shortage of labour. The elaborate plans that had been made for releasing men from the services only in accordance with the expressed needs of industry were sacrificed to political exigencies, and proved to be unnecessary. There was employment for all the labour that could be obtained in 1919, and the process of demobilisation, speedy as it was, was not speedy enough to enable production to expand to meet demand without prices rising. The result was that the boom was a price boom, not a production boom; production figures never reached 1913 level in 1919, and did not pass it until the boom was almost at an end.

In the second place, an important check, which in a more normal period would have operated to mitigate the intensity of the boom, and so to delay and to soften the subsequent fall, did not operate until its application intensified the inevitable crisis—the check, namely, of credit restriction. Before the war, under the much abused gold standard, the necessity of protecting a cash reserve, which could not be replenished by currency inflation, compelled the banks and other credit agencies to scrutinise applications and restrict credit, when it ceased to show results in increased material production and began to serve only the purposes of unnecessary speculation. This automatic check was absent in the post-war period. The gold standard was lost, and the huge floating debt not only afforded the basis for correspondingly large bank credits, but put the Government at the mercy of its creditors; if credit was restricted, the holders of Treasury bills and other Government obligations had

only to let them run out and refuse to renew them to compel the Government to borrow from the bank, and so provide the means of expanding credit again.

The optimistic finance of Mr. Bonar Law and Mr. Chamberlain, or perhaps it would be fairer to say of the Coalition Government, has a good deal to answer for. The country was under-taxed when it was prosperous; the Government preferred to increase the floating debt and to remit taxation in 1919, although it was realising hundreds of millions by the sale of war stores. The result was, first, an undesirable inflation of credit and prices; second, the necessity of raising the Excess Profits Duty a year later, at the moment when its effect in assisting depression would be greatest; and third, the very heavy pressure of taxation during the depression. The Government's financial policy served first to exaggerate the boom and then to intensify the depression.

A third abnormal condition due to the war, a condition that helped to make the boom short-lived, was that the boom did not follow a depression. The effect of depression, we saw, was to eliminate the weaker firms, to tighten up organisation, and generally to bring down costs; these were not the results that war had brought. On the contrary, profit-making had been easy, inefficient firms were numerous, the output of workers (per head) had declined, equipment—for peace purposes as distinct from munitions production—had deteriorated. The physical volume of production did not, therefore, expand to the stimulus of rising prices at the rate it would have done before the war; shortage continued throughout 1919, sending prices ever higher. And when costs followed prices and the margin of profit narrowed, industry had not the staying

power that it would have derived from the hardening and refining influences of an antecedent depression. Costs were harder to reduce, the proportion of inefficient firms that were unable to meet their contracts was greater, the resultant strain on the banks for accommodation was more sudden and extensive. The boom, it is safe to conclude, would not have come to such a sudden end if it had been based on a true increase in productive efficiency instead of on a transient condition of demand.

When the boom ended, however, instead of the situation being relieved by the bankruptcy of the weaker firms, whose management or resources were not equal to the task of reducing costs and so lifting industry out of the depression, the banks tended to carry many of these, giving them additional credit, which did not enable them to recover, but only to continue an insolvent existence in which their desperate price-cutting hampered the recovery of more solvent concerns.

Finally, the post-war boom was exceptional in the elements of uncertainty that attended it. Prices were out of step; any study of price movements between 1919 and 1923 shows how recovery waited on the convergence of series that had diverged in the boom. Relations between prices did not, therefore, afford the assistance they usually give to an estimate of the trend of prices. The underlying influences of supply and demand were equally difficult to gauge. Supplies were being constantly interrupted by labour disputes, transport delays, unexpected shortage of materials; and the problem of estimating competition was rendered the more difficult by the differing degrees of speed with which different firms effected the turnover from muni-

tions to peace production. Demand seemed insatiable, but future prospects were difficult to foresee. In the first year after the war the home market took a disproportionate share of the output of British industry as compared with before the war, and certain European markets took a disproportionate share of our exports; neither change was permanent. Wages, like prices, were difficult to gauge, and the method of trial and error that was adopted to find what wages industry could stand involved a loss of 63 million working days in the two years 1919–20, as compared with 11½ millions in 1913. Added to these economic elements of uncertainty, and as disturbing as any of them, was the novel and extensive influence of Governments on trade. The treaty negotiations and the treaty itself, with its resultant Reparations problem, would have taxed the prophetic power of omniscience itself. If it had had no other effects, therefore, the war explains the intensity of the post-war boom and the subsequent depression. And its influence in exaggerating trade fluctuation was so neglected at the time that there was for long a tendency to ignore all other effects.

IV. *Conclusion*

It is clear that one element in the post-war problem has been an exaggerated fluctuation of the same kind, though greater in degree, as pre-war fluctuations. The depression has been greater, because the boom was greater. But no conceivable exaggeration of ordinary trade fluctuation will explain certain features of post-war unemployment. Not only was the collapse of the post-war boom followed by an unprecedented volume of unemployment; more significant is the persistence of

this unprecedented volume. If ordinary trade fluctuation had been the explanation, we should have expected trade to recover after 1922 under the double influence of reviving demand and reduction of costs. Trade did recover, but not sufficiently to bring unemployment down to any figure that could be regarded as normal by pre-war standards. A closer examination will show that trade fluctuation has continued since the collapse of the boom, although its course has been obscured and diverted by such abnormal influences as the return to the gold standard and national stoppages in the coal industry. But these fluctuations have taken place on the top of a persistent depression represented by something like a million unemployed. This underlying problem has persisted so long that there is no warrant for attributing it to ordinary trade depression and expecting it to be relieved by unaided trade recovery. Trade has recovered; 1924 was a boom year, if the characteristics of a boom year are a peak in prices, production and employment. But abnormal unemployment persisted; the expansion in demand and reduction in costs, which before the war without any special action by Government relieved the worst depressions, have not gone far enough to relieve this post-war depression. It is necessary, therefore, to examine the course of unemployment since 1920, and analyse the elements in it, in order to discover other factors to account for unemployment, which the most exaggerated trade cycle will not explain.

CHAPTER II

THE COURSE OF UNEMPLOYMENT SINCE THE WAR

1. *Summary*

THE course of unemployment since the war is not difficult to follow. There is much that is controversial in the explanation of the course; but the figures supplied by the working of the unemployment insurance scheme, and the index provided by trade union unemployment schemes before the State scheme was extended to cover the greater part of industrial employment, put beyond dispute the actual time and direction of change. The rest of this chapter is given to an examination of these figures, which call for certain minor qualifications before they can be taken as an accurate index of unemployment, and a certain amount of analysis before they will reveal the divergent and compensating movements in different parts of the industrial field of which they are the result. In this first section the results of this examination will be anticipated, and the course of unemployment summarised; the remaining sections are not needed to follow the argument of the succeeding chapters, and are added only to justify this summary. Readers who are prepared to take the summary on trust may omit them.

The outstanding feature of post-war industry is the rapid increase of unemployment on the collapse in

1920–21 of the post-war boom, and the gradual recovery since. This recovery continued, without other interruption than the usual seasonal increase of unemployment in the autumn and winter, from the end of 1921 until the summer of 1924. Since that date it is difficult to discern any general trend. Employment was definitely worse in 1925 and 1926, better in 1927 and worse again in 1928; if the last half of 1928 be compared with the last half of 1924 there is an increase of unemployment from 10·6 to 11·6 per cent. It is probable, however, that the improvement in the latter half of the depression is slightly greater than the figures indicate, since legislative and administrative changes have tended to bring into the recorded figures unemployed persons who did not register as unemployed before 1924, and also employment owed more to public work, put in hand to relieve unemployment, before 1926 than it has done since.

This general movement of collapse, recovery and check has been diversified by a number of temporary or exceptional influences. The collapse of employment in 1920 and 1921, and the more gradual but still unmistakable increase in unemployment in 1925, followed in each case a fall in the general price level; and these falls in the price level were associated with decisions in monetary policy by which the country returned to the gold standard. It will be necessary to examine the connection between monetary policy and unemployment at some length in the next chapter.

The two peaks of unemployment coincided with stoppages in the coal-mining industry; and the effects of these stoppages were not confined to the period of the actual stoppage. The chief reason why it is difficult to discern the trend of employment since 1924 is that

in 1925 and the early part of 1926 employment was affected by the Coal Subsidy, during the rest of 1926 by the stoppage itself, and throughout 1927 by the accumulation of work held up in 1926 by the stoppage. Other trade disputes have had a similar though much smaller influence.

The total figures and general percentage of unemployment conceal important changes in the character of the post-war problem. In January 1922 the engineering and allied industries accounted for 15·8 per cent of all recorded unemployment, while coal accounted for only 5·8 per cent; in January 1929 the engineering group accounted for only 5·3 per cent, while coal now supplied 19·1 per cent. This is only the most marked example of changes in the constitution of the unemployed total which are continually taking place. It is necessary, therefore, to consider also the movement of unemployment in separate industries and industrial groups. There are difficulties in the way of such detailed comparisons; but certain movements are clear. Before 1925 the chief element in our problem was the unemployment in the metal and engineering industries, which had been expanded to meet the war-time demand for munitions and ships; since 1924 the biggest single contributor has been the coal industry. In the earlier years, again, building contributed largely to unemployment; from 1923 to 1928 building activity did much to relieve unemployment; latterly, building has risen to a position second only to coal, as a contributor to unemployment. Had the depression in coal come at the same time as the depression in the engineering and metal group, the contrast between the first half and the second half of the post-war depression would have been much more marked than it is; had the

unemployment problem of the metal and engineering group not been relieved after 1925—mainly by a reduction in the numbers dependent for work on these industries—the period 1925–28 would have been as bad as 1921–23. Improvement in one industry has been cancelled out by deterioration in another, and underneath the general upward and downward movement of industrial activity there are these divergent and compensating movements of particular industries.

No single general explanation, therefore, will account for the changes in industrial activity that the unemployment figures reflect. There are general influences that affect all industries; but each industry also is subject to special and peculiar influences that need separate examination. After the examination of the most obvious general influence, that of monetary policy, which will be made in the next chapter, it will be necessary to distinguish and classify the more important particular influences, affecting particular industries, which have made of post-war unemployment a bundle of distinct, though related, industrial problems.

Two further inferences can be drawn from the statistics of unemployment; and one important limitation on their usefulness requires mention. Their chief use is to reveal and measure variations in the amount of unemployment, for which purpose they are quite adequate. They will also, although they serve only as a rough indication, throw some light on the comparative *absolute* amounts of unemployment before the war and since. Since December 1920 the average percentage of unemployment in the insured industries has been 12. It was necessary for the purposes of the Unemployment Insurance Scheme to estimate the corresponding average amount of unemployment before the war; the

official estimate was $4\frac{1}{2}$ per cent. The difference, $7\frac{1}{2}$ per cent, the equivalent to-day of 900,000 persons, may be taken as a rough indication of the specific addition to unemployment which must be attributed to the effects of the war. It is additional to the unemployment due to ordinary trade fluctuation and the other factors which caused unemployment before the war and are still operative.

The second inference, which is the subject of the last section of this chapter, is the incidence of distress on different localities. The most depressed industries are also the most localised industries; so that the distress caused by unemployment is concentrated on a limited number of areas in which its effects are cumulative. The distress, which the national system of unemployment insurance has been unable to prevent, is found mainly in these areas.

The limitation on the usefulness of the figures, which is also treated of in the last section, is that they do not indicate the insecurity of much of the employment now being given. Some work at a loss is in the ordinary course of industry; but the high proportion of work being done at a loss or no profit, in such industries as coal, cotton and engineering, constitutes a threat to much of the employment still afforded by these industries.

II. *The Unemployment Insurance Figures*

Fortunately (or unfortunately) the statistics of unemployment are more comprehensive in the United Kingdom than in any other country.[1] We possess,

[1] I have incorporated in this section and in section i. of Chapter V. parts of a paper read before the Manchester Statistical Society on November 21, 1928.

however, no figures of unemployment for industry as a whole, and no satisfactory index that covers the whole of the ten years. Three indices are available that between them cover the greater part of the field. The first is the percentage of members unemployed in certain trade unions that pay out-of-work benefit. This was the chief index on which we relied before the war, figures for some unions being available as far back as 1854. It was a fair index of the *time* and *direction* of changes in employment, but was unreliable as an index of the *extent* of unemployment. The sample of the wage-earning population afforded was not unbiassed; unions in the engineering and constructional trades had a weight in it disproportionate to their weight in the population as a whole, and, within the industries represented, the fact that figures were drawn exclusively from trade unions involved an under-representation of unskilled and semi-skilled workers. Mr. Hilton, in an interesting paper in *The Statistical Journal* for March 1923, which is also the authority for unemployment statistics derived from insurance, recalculated the trade union index, taking the rates of unemployment as given by the experience of the unions in the different industries, but giving to these separate percentages weights in the general index based, not upon the membership of the unions, but upon the numbers in the trades represented by the unions; the result was to bring the index, for the period for which they overlap, into closer accord with the index afforded by the Unemployment Insurance Scheme. The Ministry of Labour discontinued publishing the trade union index at the end of 1926, so that it is available for only part of our period.

The Unemployment Insurance Scheme is the source

of the second index. The scheme provides that an insured person who claims benefit shall "lodge" his insurance book with an Employment Exchange. The file of books so lodged thus furnishes a record of unemployment among insured persons; since books are coded according to the industry in which the holder is engaged, it furnishes also a measure of the distribution of unemployment among different industries. The books of persons known to be sick, deceased, emigrated or transferred to an employment outside the scope of the insurance scheme are excluded from the file, as are also the books of insured persons disqualified for benefit by participation in a trade dispute. Where information is lacking on these points, a book is kept in a special file for two months, and then excluded from the unemployed figures.

The "numbers of insured persons recorded as unemployed" published in the *Labour Gazette* each month as a result of this count is the most comprehensive and accurate record of unemployment that this, or, indeed, any other country has ever possessed. It is not, however, complete or continuous throughout our period. It is not complete, because certain occupations, in which the risk of unemployment is thought to be slight, are excluded; domestic service, agriculture, and certain branches of railway work and work for public authorities, are the chief. Juveniles under sixteen, persons over sixty-five years of age (since January 1928), and employees in receipt of more than £250 a year who are not manual workers, are also excluded. The figures refer, therefore, to about three-quarters of the wage-earning population only, and are not sufficient by themselves to measure the *extent* of unemployment. They would provide an adequate index of variations if

they were continuous; but there have been several breaks in comparability.

(i.) The scheme was extended to the industrial population generally only in 1920, so that it is only since December in that year that the index is of general reference.

(ii.) On April 1, 1922, the Irish Free State took over insurance in its territory, thus reducing the numbers in the British scheme by 350,000 to 400,000.

(iii.) The treatment of short-time has varied. Until October 1922 persons working "organised short-time" were stated separately; from November 1922 to May 1923 only the number of persons totally unemployed was given; from June 1923 to March 1924 a figure was given which included totally unemployed and a proportion of organised short-time workers, but no separate figures for the latter; since then the number given has been that of persons unemployed on the day of the count, whether totally unemployed or temporarily stopped, though these two categories are also given separately.

(iv.) The basis of classification was changed at the reissue of books in July 1923. Until then the classification had been occupational, into 63 groups; it was then placed upon an industrial basis, similar to that of the census industrial classification, and the number of groups increased to 100. Since then the figures have afforded a very accurate index of the growth and activity of different industries, but it is not possible to relate accurately the later figures to the figures before July 1923.

The third possible index is the number of persons registered with the Employment Exchanges, a figure published weekly. This is perhaps the most compre-

hensive figure we have, and covers the longest range of time in our period. It is, however—like the previous figures—influenced by the scope and administrative requirements of the insurance scheme, since the majority of persons registering do so to comply with the conditions of benefit. It includes also, moreover, persons who are not unemployed, but desire to change their employment; and there is no means of ascertaining what proportion it bears to the employed population at any time, since it includes persons from uninsured as well as from insured occupations, but does not necessarily include all the unemployed persons in uninsured occupations.

The Ministry of Labour has recalculated the second figure, that based upon the insurance statistics, on a uniform basis (19th *Abstract of Labour Statistics*, p. 44) for Great Britain and Northern Ireland back to December 1921, and for Great Britain alone back to December 1920. The latter is probably the best single index of the movement of unemployment available, and is given in Table I.; to bridge the gap between the end of the war and December 1920, I give also the trade union unemployment percentage, as recalculated by Mr. Hilton.

It will be seen that unemployment, already serious at the end of 1920, increased rapidly to a peak of 23 per cent in May 1921, and, after a temporary recovery, to 17·7 per cent in December. There was then a steady recovery, which brought the percentage down to 9·3 in May 1924; if allowance be made for the seasonal rise in the latter half of the year, the recovery may be said to have continued until the end of 1924. In 1925 employment was worse, but recovered in the first half of 1926, only to rise to a new peak in June 1926. There was improvement again in 1927; 1928 was rather worse

TABLE I

UNEMPLOYMENT SINCE THE ARMISTICE

Month.	Year.												
	1918.	1919.	1920.	1921.		1922.		1923.	1924.	1925.	1926.	1927.	1928.
January	(a) ..	(a) 2·3	(a) 2·0	(a) 6·4	(b) 11·0	(a) 14·2	(c) 17·7	(c) 13·3	(c) 11·9	(c) 11·2	(c) 11·1	(c) 12·1	(c) 10·7
February	..	2·7	1·2	8·0	12·9	13·7	17·1	12·4	10·6	11·3	10·5	10·9	10·4
March	..	2·7	0·9	9·4	15·0	14·0	16·0	11·7	9·8	11·1	9·8	9·9	9·5
April	..	2·5	0·8	14·8	19·9	14·4	15·9	11·5	9·7	10·9	9·2	9·4	9·5
May	..	1·8	0·9	19·3	23·0	13·6	14·6	11·2	9·4	10·9	14·5	8·8	9·8
June	..	1·5	1·0	19·9	21·9	13·0	13·7	11·3	9·3	11·9	14·7	8·9	10·7
July	..	1·9	1·2	15·5	17·4	12·6	13·1	11·6	9·8	11·2	14·6	9·3	11·6
August	..	2·2	1·3	15·0	15·1	11·9	12·8	11·8	10·5	12·1	14·2	9·4	11·6
September	..	1·5	1·9	13·1	13·9	11·8	12·7	11·7	10·6	12·0	13·9	9·4	11·4
October	..	1·9	4·1	13·8	14·3	11·6	12·6	11·7	10·9	11·4	13·6	9·5	11·8
November	0·5	2·0	3·3	13·7	16·9	11·5	13·0	11·5	10·8	11·0	13·5	10·0	12·2
December	1·1	2·2	5·6	13·5	17·7	11·2	12·8	10·6	10·7	10·5	11·9	9·8	11·2

a Trade Union Unemployment Percentage as corrected for True Occupational Distribution by Mr. Hilton (v. *Statistical Journal*, March 1923, pp. 190-1).

b Percentage of insured workpeople unemployed in Great Britain.

c Percentage of insured workpeople unemployed in Great Britain and Northern Ireland.

than 1927, and the first three months of 1929, although showing the usual seasonal improvement, were worse than the corresponding months of 1928.

The course of employment revealed by these figures has obviously been influenced by certain temporary and abnormal factors.[1] The two peaks of unemployment correspond with national stoppages in the coal-mining industry, and the rise in each case, from prosperity in 1920 and from comparative prosperity in 1924, corresponded with an important decision on

[1] Recorded unemployment may misrepresent actual unemployment, because the legislative and administrative requirements that lead unemployed persons to register, and so to record their unemployment, are altered. Thus, the recovery indicated by recorded unemployment in September and October 1921 may be deceptive and exaggerated, being accounted for in part by the removal from the record of persons who, having exhausted rights to benefit under the insurance scheme, did not trouble to maintain registration at the Employment Exchanges. Again, in April 1923, February 1924, and August 1924, the conditions of benefit were relaxed; in February and July 1925 the conditions were made more stringent again. The Balfour Committee (*Interim Report on Industrial Relations*, p. 230) gives an estimate of the number of persons added to the *recorded* figures of unemployment by the Act of August 1924 as 70,000; a careful examination of the effects of the changes made in 1925 (Cmd. 2601) put the maximum reduction in recorded unemployment due to those changes at 13,000, which would imply that the figures since 1925 have been inflated by 60,000. Since, however, the main purpose of the 1925 changes was to reverse the 1924 changes, it is more probable that 70,000 is an overestimate, and the net inflation of the figures smaller than 60,000. A further relaxation of conditions of benefit in April 1928 may have added 40,000 to the number recorded as unemployed, and the institution in July of the system of franking the Health Insurance cards of persons registered at Employment Exchanges another 25,000. It is impossible to say to what extent these increases and decreases persisted; so that they are not necessarily additive. In any case the actual effect of these administrative changes upon the figures is likely to be less than the maximum possible, since the figures measure, not the number of persons in receipt of benefit, which is, of course, seriously affected, but the numbers recorded as unemployed, because they register; and registration must have become a general habit of the unemployed, even when out of benefit, since they can never be sure that some new measure will not put them into benefit again. The maximum change, 135,000, would be equivalent to little more than 1 per cent of the insured population. Minor changes were the inclusion of unemployed persons under the two Special Schemes in Insurance and Banking, an addition at the time of 7000 only, and the exclusion in January of this year of persons aged 65 and over, estimated then at 30,000; since the same class of persons was excluded from the figures of the insured population, the result was to leave the general percentage of unemployment practically unaffected.

monetary policy made by the Government of the day. The fluctuations revealed cannot, therefore, be attributed simply to the influences which brought about trade fluctuation before the war, and they have not the regularity that pre-war fluctuations tended to show. The boom of 1919–20 was followed by the slump of 1921–22, and that by a distinct recovery; but recovery was checked before it had brought unemployment down to the dimensions of a bad year in a pre-war depression, and since then it has been difficult to say whether the tendency of employment has been to improve or to get worse. Something can, however, be done to mark and disentangle the influence of these temporary and abnormal factors.

The influence of monetary policy will be examined in the next chapter; here it will be sufficient to note the outstanding facts. Just as in pre-war fluctuations, there has been a general correspondence between the movement of prices and the movement of employment. Rising prices in 1919 and 1920 were accompanied by intense industrial activity; the fall in prices in 1920 and 1921 by a corresponding increase in unemployment. The gradual rise in the price level from 1922 to the end of 1924 saw a steady improvement in employment, while the subsequent fall was followed, though rather irregularly, by a renewed falling off in employment.

While there has been this general correspondence between prices and employment, there have been one or two divergences in detail that may be significant. Thus before the war the movement in employment tended to precede the movement of prices; in 1920 prices broke five months before employment gave way, and employment began to revive in January 1922, while prices did not turn upwards until October

of that year. Then there appears to be a seasonal divergence of prices and employment in the winter, which was exaggerated and extended to the whole year between July 1924 and June 1927. However, even on the theory that trade fluctuations are purely a monetary phenomenon, an exact correspondence of prices and employment could not be expected; for the index of employment refers to British manufacturing and mining industry, while the index of prices is based largely on prices of imported food-stuffs and raw materials. Moreover, industrial activity and the consequent course of employment have been subjected in the last decade to other handicaps and interruptions, to which we must now turn.

III. *Special Influences*

Persons unemployed as a result of a trade dispute in their own trade are not entitled to benefit, and are excluded from the figures of unemployment.[1] Persons may, however, become unemployed as a result of a dispute outside their own industry. Before considering the effect of the stoppages in coal it may be noted that a recession of employment in the autumn of 1919 was partly caused by the short railway strike and the more obstinate moulders' strike, that began in September, and that another railway stoppage inflated the figures of unemployment in January 1924.

None of these, however, had the influence of the mining stoppages. That of October 1920 had only a temporary, though an obvious effect; the influence of the two more prolonged national disputes, from April to June (inclusive) 1921, and from May to November

[1] Although those workpeople in the affected trades who were unemployed when the dispute began do not lose their rights to benefit, and continue to figure in the total of recorded unemployment.

(inclusive) 1926, was felt before the actual stoppage began, and continued after it was ended. Before the stoppage, while employment might be stimulated by the endeavour to accumulate supplies, the restriction of enterprise which the probability of a stoppage entailed would have the opposite effect. After the stoppage employment would be temporarily expanded by the accumulation of work which the stoppage involved. In 1925 a special influence was exerted by the subsidy which the Government granted pending an inquiry, particularly upon the coal and heavy industries; these were sinking into a renewed depression when the subsidy revived them. In reviewing the course of employment, then, we must allow for these influences. We shall put the lowest point of the post-war depression, not in May, but in December 1921, and we shall discount the apparent recovery in September and October. We shall attribute the improvement in the figures between August and December 1925, when we should have expected a seasonal increase in unemployment, to the operation of the Coal Subsidy, which would also account for part of the further improvement to April 1926. The rise in unemployment for the rest of 1926 we can attribute to the mining stoppage, and a considerable part of the improvement in the first half of 1927 must be accounted for by the accumulation, during the stoppage, of work that could be postponed. Not until 1928 was it safe to accept the unemployment percentage as indicative of the true trend of employment.

IV. *Distribution by Industries*

Averages are deceptive, and the general percentage of unemployment in insured industry as a whole may

conceal divergent and compensating movements of employment in different industries or industrial groups. An indication of the changes in the constitution of the unemployed total is given in the following table:

TABLE II

PERCENTAGE DISTRIBUTION OF RECORDED UNEMPLOYED AT END OF JANUARY IN EACH YEAR

Percentage of all Unemployed in

	Coal.	Engineering and Allied Industries.	Iron and Steel.	Ship-building.	Cotton.	Building.	Percentage of Insured Population Unemployed.
1921	0·7	11·2	2·7	2·4	13·9	6·0	11·0
1922	5·8	15·8	5·5	6·2	6·2	8·6	17·0
1923*	3·75	15·7	4·1	8·3	4·7	10·4	12·7
1924	4·2	11·8	4·4	6·4	6·6	8·0	11·9
1925	7·6	9·2	5·5	6·1	2·6	7·2	11·2
1926	9·6	8·8	4·3	6·8	3·6	8·5	11·0
1927	13·8	9·0	3·5	5·7	4·5	8·5	12·0
1928	16·7	6·7	4·1	3·4	4·4	11·2	10·7
1929	14·5	6·5	3·0	3·8	4·3	11·1	12·3

* Totally unemployed only.

PERCENTAGE OF INSURED POPULATION (EMPLOYED AND UNEMPLOYED) IN EACH INDUSTRY AT JULY IN EACH YEAR

	Coal.	Engineering and Allied Industries.	Iron and Steel.	Ship-building.	Cotton.	Building.	
1921	9·3	10·2	2·4	2·8	4·3	7·0	
1923	10·8	9·0	2·6	2·35	4·9	6·2	
1927	9·9	7·7	2·3	1·8	4·7	7·0	
1928	9·4	7·8	1·9	1·7	4·6	6·8	

NOTE.—The figures for 1921 and 1922 are not exactly comparable with those for 1923 and subsequent years, because they refer to the United Kingdom, while the latter refer to Great Britain and Northern Ireland; and the figures for 1921–23 are not exactly comparable with those of 1924–25 because they are based on an "occupational" classification, while the latter are on an "industrial" classification. The figures for different industries in any one year are, however, comparable.

It is clear that the percentage for insured industry as a whole requires to be supplemented by an examination of the changes in the percentage unemployed in each important industry or group of industries.

Unfortunately breaks in comparability of the figures for separate industries make it impossible to get a continuous index of unemployment in any industry, even from 1921. Since June 1923, however, there has been no change of importance, and figures for the earlier period, which are comparable within that period, are available. A rough comparison can therefore be made of the movement of employment in different industries. This is done in the following table, which gives, for the end of each quarter, the unemployment percentage for certain important industries and industrial groups, and also the divergence of that percentage from the general percentage for all insured industry.[1]

[1] The table should be read with the following cautions:

1. There are breaks in comparability in March 1922, after which month the Irish Free State is excluded; in October 1922, after which month until June 1923, no separate figures of organised short-time workers are given; in June 1923, when the insured population was reclassified on an "industrial" basis and allowance was made again for short time; and in March 1924, after which month the figure of unemployment has included only those short-time workers who happened to be unemployed on the day of the count.

2. It was necessary to make some allowance for short time in the index of unemployment, in the period before the Ministry of Labour gave a single figure, since in some industries the greater part of unemployment took the form of short-time working. The conditions of benefit required an applicant to prove continuous unemployment, or alternatively two periods of unemployment of not less than two days each, separated by a period of not more than two days of employment, or two periods of unemployment of not less than six days each, separated by not more than six weeks' employment. I have assumed from this provision that two organised short-time workers were about equivalent to one wholly unemployed worker for the purpose of this present table, and have treated them as such in the period December 1920 to September 1922.

3. I have grouped together in the period after June 1923, under the head of "Engineering and Allied Industries", the industries separately distinguished since that date, as "Engineering; Engineers' Iron and Steel-Founding", "Electrical Engineering", "Marine Engineering, etc.", "Constructional Engineering", "General Iron-Founding", "Electrical Cable, Wire and Electric Lamp Manufacture", and "Heating and Domestic Engineering". This I have done because separate figures were not given for these different branches of Engineering before June 1923; even so, the group does not correspond exactly with the heading "Engineering and Iron-Founding" in the pre-1923 classification; since certain workers formerly classified under Engineering were transferred to the Motor Vehicle group. In addition, the change from the occupational to the industrial basis of classification makes a direct comparison impossible.

TABLE III

UNEMPLOYMENT PERCENTAGES AND DIVERGENCE FROM GENERAL PERCENTAGE IN CERTAIN INDUSTRIES

Date.	General Percentage of Unemployment.	Coal.		Engineering and Allied Industries.		Cotton.		Building.	
		Per cent.	Divergence.	Per cent.	Divergence.	Per cent.	Divergence.	Per cent.	Divergence.
December 1920	7·8	0·3	− 7·5	8·8	+ 1·0	27	+ 20	7·0	− 0·8
March 1921	15·0	2·3	− 12·7	16·2	+ 1·2	42	+ 27	9·8	− 5·2
June	21·9	*	*	31·0	+ 9·1	*	*	15·9	− 6·0
September	13·9	10·2	− 2·7	23·6	+ 9·7	13	− 0·9	14·4	+ 0·5
December	17·7	11·2	− 6·5	29·3	+ 11·6	24	+ 6·3	20·8	+ 3·1
March 1922	15·8	8·1	− 7·7	28·5	+ 12·7	20	+ 4·2	18·3	+ 2·5
June	12·9	8·7	− 4·2	26·0	+ 13·1	8	− 4·9	15·2	− 2·3
September	12·5	6·0	− 6·5	23·4	+ 10·9	7	− 5·5	15·2	− 2·7
December	12·2	4·6	− 7·6	20·6	+ 8·0	9	− 3·2	18·5	+ 6·3
March 1923	11·1	3·6	− 7·5	17·6	+ 6·5	14	+ 2·9	15·1	+ 4·0
June	11·2	2·5	− 8·7	17·6	+ 6·4	21·2	+ 10·0	12·5	+ 1·3
September	11·6	3·1	− 8·5	17·8	+ 6·2	20·1	+ 8·5	11·9	+ 0·3
December	10·5	2·4	− 8·1	16·0	+ 5·5	12·0	+ 1·5	13·6	+ 3·1
March 1924	9·7	2·1	− 7·4	15·7	+ 6·5	15·4	+ 5·9	10·1	+ 0·6
June	9·2	4·7	− 4·5	13·2	+ 4·0	15·2	+ 6·0	8·2	− 1·0
September	10·5	8·2	− 2·3	14·4	+ 3·9	14·3	+ 3·8	9·7	− 0·8
December	10·6	7·8	− 2·8	12·4	+ 1·8	7·0	− 3·6	11·8	+ 1·2
March 1925	10·8	11·9	+ 1·1	11·9	+ 1·1	7·2	− 3·6	9·5	− 1·3
June	11·6	25·4	+ 13·8	11·5	− 0·1	8·7	− 2·9	7·4	− 4·2
September	11·7	23·6	+ 11·9	11·7	0	10·2	− 1·5	8·4	− 3·3
December	10·1	11·2	+ 1·1	11·3	+ 1·2	6·7	− 3·4	13·3	+ 3·2
March 1926	9·5	9·4	− 0·1	11·8	+ 2·3	9·7	+ 0·2	8·5	− 1·0
June	14·3	*	*	17·3	+ 3·0	25·1	+ 10·8	9·5	− 4·8
September	13·5	*	*	16·8	+ 3·3	24·3	+ 10·8	10·1	− 3·4
December	11·7	10·2	− 1·5	14·8	+ 3·1	13·3	+ 1·6	13·5	+ 1·8
March 1927	9·7	16·8	+ 7·1	11·3	+ 1·6	6·0	− 3·7	9·4	− 0·3
June	8·8	19·1	+ 10·3	9·4	+ 0·6	7·0	− 1·8	6·9	− 1·9
September	9·2	19·1	+ 9·9	9·0	− 0·2	9·3	+ 0·1	9·1	− 0·1
December	9·8	17·3	+ 7·5	8·7	− 1·1	10·0	+ 0·2	16·0	+ 6·2
March 1928	9·6	17·2	+ 7·6	9·2	− 0·4	9·2	− 0·4	11·3	+ 1·7
June	10·8	25·7	+ 14·9	9·4	− 1·4	12·9	+ 2·1	10·5	− 0·8
September	11·5	21·6	+ 10·1	9·9	− 1·7	14·3	+ 2·8	11·7	+ 0·2

* Stoppage in the industry.

The significance of this table will be appreciated more easily from Fig. 4, in which the divergence of unemployment in the industries tabulated (and certain others) from the percentage of unemployment in the insured population as a whole is presented graphically. The general percentage is represented by the straight broken line in each case, and the divergence of the percentage in the separate industries by the continuous line. The percentage scale of each industry is so adjusted that the same vertical distance on any of the scales represents the same number of persons in 1923. A study of this figure brings out clearly the fact that divergent and compensating movements have been important. With the exception of building, none of the industries represented has followed the general trend of employment; all have been subject to influences that affected them alone or in a peculiar degree. The general level, and the changes in the general level, of unemployment in the country cannot be completely explained by any diffused influence or influences affecting all industries simultaneously and in like degree.

A note on each of the industries tabulated will further illustrate this point.

1. The coal industry recovered with comparative rapidity from the dislocation caused by the 1921 stoppage, and until the beginning of 1925 had an unemployment percentage better than the average. This was, however, due to the transient circumstances that German production was hampered by currency and other internal disorders in 1922, and by the French occupation of the Ruhr in 1923 and 1924. Between 1922 and 1926 German unemployment, as indicated by trade union returns, varied inversely as British unemployment, since the circumstances that affected the

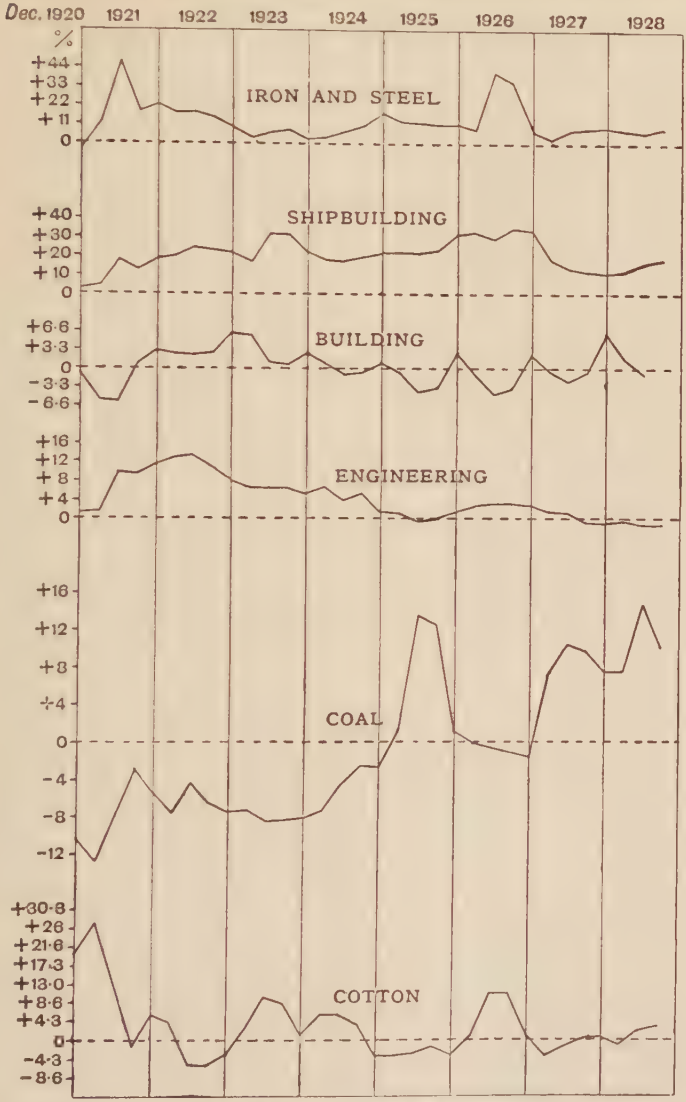

Fig. 4.—Divergence of Unemployment in certain Industries from General Percentages.

coal-mining industry affected also the other "heavy" industries. By 1925, German output had recovered,

and, since the European demand for coal, at prices that will cover the present wages, is not large enough to keep all the European miners employed, some country's mining industry has had to suffer, and ours, as the largest, has suffered most.

2. The engineering group shows a steady improvement, interrupted only by the 1926 coal stoppage, from the depths of the depression in the winter of 1921–1922 until the end of 1927. In 1921 and 1922 it was the largest contributor to the unemployed total; since 1925 its condition has been about average. The explanation here is obvious, and is the explanation also of the excessive unemployment and gradual improvement in iron and steel and shipbuilding. The war brought about an abnormal expansion in these industries (nearly 50 per cent in the engineering group), and the unemployment percentage has been reduced by a reduction in the number of persons seeking employment in them.

3. The cotton industry has pursued a path of its own. The collapse of the Eastern markets in 1920, with the fall in the sterling value of rupees and silver, produced the first great depression, from which the industry has never recovered, although there was a temporary recovery in the winter of 1924–25 and the first half of 1927.

4. Building has been the recipient of a succession of favours from the Government in.the form of subsidies, the benefits of which were reduced by their intermittent and irregular character. The net result has been, however, that building has been about as busy as industry generally, the chief feature of the industry being a marked seasonal increase of unemployment in the winter. This summary is, however, true only of the

industry as a whole; were we to consider the employment of skilled artisans and labourers in the industry separately, we should find very different experiences.

The general conclusion to which this partial analysis of the general unemployment figure into its constituent elements points, is that the post-war problem, whatever general influences have operated to create it, is in part to be explained as a bundle of separate and distinct, if connected, problems affecting separate industries. After the war it was the abnormal expansion of the metal industries; now it is the excessive personnel of the mining industry. Cotton has its separate problem; building its problem of an excessive proportion of labourers. Making allowance for these special influences, we should discount the improvement which the general figure shows in 1923 and 1924 as being in part due to the Ruhr occupation; German industry was, however, recovering before the occupation was terminated, and the summer of 1924 must still be considered one of the best, if not the best, quarters since 1920. The spring of 1926 and the spring and summer of 1927 showed even better figures, but these were influenced, the one by the Coal Subsidy, the other by the accumulation of orders carried over from the 1926 stoppage.

A factor that affects slightly any comparison between the earlier and later parts of the depression is the extent of employment provided by relief works or other public works specially instituted to relieve unemployment. Unfortunately recent estimates are not available, but it is probable that the number is less than the 110,000 estimated to be so employed in January 1926, or the 91,000 estimated for October 1924. The improvement in ordinary commercial em-

ployment on this showing would be rather greater than the figures of recorded unemployment would suggest. The effects of administrative and legislative changes upon the figures [1] tend in the same direction.

v. *The Residual Post-War Problem*

It will be noticed that every improvement in the industrial situation—in 1924, in 1926 (before the coal lock-out), in 1927, in 1928, stops short at a figure of $8\frac{1}{2}$ or 9 per cent of unemployment, representing a million persons or a little over. The figures, as has been explained, do not cover the whole of wage-earning employment, so that, although a reliable index of variations, they do not measure the absolute amount of unemployment. They do, however, throw some light on the question, how does post-war unemployment compare in amount with pre-war unemployment.

The Unemployment Insurance Scheme, in its present extent, dates only from 1920; there is, therefore, no pre-war figure corresponding exactly with the post-war unemployment percentage which it supplies. It was, however, necessary to make an estimate of the average risk of unemployment under normal conditions in order to provide an actuarial basis for the 1920 Unemployment Insurance Act. This had to be based upon pre-war experience, and the Government Actuary, using trade union records of unemployment and such other material as the Ministry of Labour could collect, estimated the *average* rate of unemployment before the war, for the trades now insured, at a little over $4\frac{1}{2}$ per cent, the equivalent of rather more than

[1] Cf. footnote on p. 35 *supra*.

half a million persons.[1] The average since the end of 1920, when the extended insurance scheme came into operation, has been 12·1 per cent, the equivalent now of 1,450,000 persons. The difference between the official estimate of pre-war unemployment and this post-war average, 7½ per cent, representing 900,000 persons in the insured trades, is as good an indication as we can get of the magnitude of the specific post-war problem, which is to be attributed not to industrial fluctuations and other influences that were operative before the war, but in one way or another to the war.

The same result is obtained by comparing the post-war *minimum* of 8½ per cent with the pre-war *minimum*. The trade union unemployment index did not fall below 1·7 per cent in any month in the twenty years before the war; this percentage would represent about 200,000 persons in the insured trades to-day. The trades covered by the trade union index before the war fluctuated more widely than industry in general, so that the minimum percentage for industry as a whole would not be less than 1·7 per cent. The difference between this pre-war and the post-war minimum would represent about 800,000 persons to-day, a figure sufficiently near the figure reached by the other comparison to support it.

The problem is, however, not stationary, and some progress would appear to have been made in dealing with it. If the post-war depression be divided into two parts, 1921–24 and 1925–28, the average unemployment percentage of the second part was only 10·9 as compared with 13·5 in the first part. This reduction

[1] Report of (Blanesburgh) Unemployment Insurance Committee (1927), I, 89. It should be noted that the Government Actuary did not put forward this as a percentage that should be regarded as normal under post-war conditions.

represents an improvement of, roughly, 300,000 in the number of persons employed, and reduces the specific war problem to between half and three-quarters of a million. It is interesting, and probably significant, to compare this aggregate reduction with the reduction in the number of unemployed in the metal and engineering industries expanded by the war, a reduction effected, not by any marked increase in employment, but by the contraction in the numbers engaged in these industries. Between June 1923, when the present "industrial" classification of the insured population was adopted, and June 1928, the number of recorded unemployed in engineering, shipbuilding, iron and steel fell from 353,000 to 186,000; in the same period the numbers of persons recorded as insured in those industries fell from 1598 to 1411. Evidently a spontaneous adjustment of labour to the changed conditions brought about by the war has been taking place in the industries in which it was needed most.

VI. *The Social Effects of Unemployment*

In one important respect the unemployment insurance figures conceal the true gravity of the problem. A certain amount of production at all times is carried on at a loss, and in the deepest depression some firms contrive to earn a profit on some or all of their output. But the present position in some of the depressed industries, even after all possible recognition of recent improvement, is abnormal and unstable. The only industry for which comprehensive statistics are available is the coal-mining industry, in which the average loss per ton disposable in the last two years has been 5·8 pence and 11 pence respectively; this in spite of an

extension of hours by a seventh, a reduction of wages per shift by an eighth, and a reduction in numbers employed by 160,000, since 1925. Yearly figures here conceal improvement, since the loss in the last quarter of 1928 averaged only 2·87 pence per ton; but a loss was still being made on the output as a whole of every coal-field, and was still upwards of 6 pence per ton in the main depressed fields. Moreover, while a part of the industry was being restored to a profitable basis, it would appear that such profits could be maintained only by a further contraction in the industry, since the most prosperous area, covered by the Five Counties Scheme of price and output regulation, has recently announced a reduction in the quota which constituent pits were permitted to produce for the summer quarter. And most of the wage agreements under which the present low rates of wages are paid expire in December 1929. Even the contracted area of employment which the industry offers is not secure; if nothing can be done to restore the industry to a profitable basis, a further contraction must be expected.

The cotton industry is in a similar position. A large part of the diminished employment at present given is given only at a loss. Here there are no comprehensive statistics; but the Lancashire Cotton Corporation, which is endeavouring to form a merger of the firms spinning American cotton, has published the results of its inspection of the balance sheets of 200 mills, which have been submitted to it. These comprise 19¾ million spindles, nearly half the spindles engaged on American cotton in the country, in addition to 28,000 looms; they have a total debt of £28,980,000, on which interest at 6 per cent calls for £1,733,000 a year. So

far from covering this charge, the companies are making (on a fair allowance for depreciation) a loss of £340,000 a year, so that the burden of indebtedness is increasing at the rate of £2,000,000 a year. It is significant also that the spinners of Egyptian cotton, who until the last year have been little affected by the depression, have in 1928 in many cases shown losses, and for a time adopted a policy of organised short-time working in order to relieve the congestion of stocks. The weaving branch of the industry, although no comparable figures are available, is probably also unprofitable; while the finishing trades, if profitable still, can continue to give employment only in proportion to the yarn and cloth sent to them by the spinning and weaving sections for processing.

Other industries give occasional indications of the same tendency. Thus figures were quoted, in negotiations over wages between the Engineering Employers' Federation and the unions in April 1928, of the average profit earned on output (selling value of product) from 1923 to 1927. The percentages were 2·52 for 1923, 1·85 for 1924, 2·85 for 1925, 2·04 for 1926, and 2·7 for 1927. An average figure of this order of magnitude, upon an output of £180,000,000 to £200,000,000 a year, implies a good deal of work done at a loss, and there is no obvious trend to a better state of things revealed. The proportion of the work done for export markets was given in the same discussions; in percentages for the successive years it was—18·4, 27·6, 25·8, 28·2, 27·0. It would appear that the engineering group was holding its own in foreign markets, but not making much progress in recovering its pre-war position.

The problem, then, is not immediately one of recovering lost opportunities of employment, but of

making secure those that are still afforded by the depressed industries. The second factor of which account must be taken is the local concentration of unemployment.

We get a very imperfect—indeed a misleading—idea of the unemployment of the last few years if we look only at the unemployment figures for industry as a whole. At the last count of the unemployed last year, in industries covered by the National Unemployment Scheme, the percentage of unemployment for Great Britain as a whole was 11·1; by the end of March the figure had improved to just 10. Now it is serious enough that one in nine—or one in ten, to take the later figure—of the workers of the country should be out of work; but the social and human effects of this unemployment follow very largely from the uneven distribution, from the *concentration* of unemployment in a limited number of industries and a limited number of districts. The thirteen hundred thousand unemployed were not distributed evenly over all the industries and the whole country; in some important industries not one in twenty of the working population was out of work, in others the proportion was one in three; in some districts unemployment was negligible, in some every other man was out of work. We must look then at the distribution of this burden of unemployment.

It is an unfortunate fact that unemployment is worst in those industries that are most highly localised; and the peculiar hardships and the special difficulties of the post-war problem spring largely from this fact. The losses and strain that industrial depression involves have not been distributed evenly over the whole community, but concentrated on the districts in which the depressed industries are localised. The most

depressed of the greater industries in recent years have been shipbuilding, iron and steel, coal, and the older textile industries—cotton, wool and linen. Among the smaller industries tin-plate, cutlery, pottery may be mentioned. All these are highly concentrated in particular localities which are mainly dependent upon them. The coal-fields are the most striking example, since the greater part of the coal of the country is mined in districts which have no other important industry. But shipbuilding is even more concentrated, with the result that the Clyde, the North-East Coast and Barrow have shown an even higher degree of depression than some of the coal-fields. In other districts, while there is not the same dependence on a single industry, there is depression in two or more industries. In South-East Lancashire the cotton industry is even more important than coal, but unfortunately equally depressed. The West Riding has had to face depression in coal, wool, heavy engineering and steel simultaneously. Before the war the expanding coal industry of Durham and Northumberland provided an outlet for the surplus population of Newcastle and the other shipbuilding centres; since the war both have had a surplus that neither can absorb.

The results of this concentration are seen in the incidence of distress relieved by the Poor Law. There are 630 Poor Law Unions in England and Wales; 400 of these have not been touched by the problem of able-bodied pauperism. On the other hand 50 unions, with 35 per cent of the population, account for more than four-fifths of the able-bodied pauperism of the country. A secondary effect is seen in the burden of rates. In Newcastle, for example, rate expenditure per head of

population rose between 1913 and 1914 from 34s. 3d. to 87s. 1d., but Poor Law expenditure rose from 6s. 3d. to 35s. 7d. Other Tyneside districts show a similar growth. Where the average burden of poor relief per household before the war was 25s. or 30s. it is now 90s. to 150s. In spite of differences in administration, the chief explanation of high rates is intensity of need and lack of rateable resources.

The statistics of unemployment illustrate even more clearly the concentration and uneven incidence of the problem. At the end of last year a quarter of the population were in counties with less than 5 per cent of unemployment; while Durham and the four southern counties of Wales had all more than 20 per cent of unemployment. London, with four times the population of Durham, had fewer unemployed. Of the counties south of the Thames, only Cornwall had more than 10 per cent; of the counties north-west of the Trent and Severn, only Westmorland had less than 10. Similar differences are found within each county. Lancashire had an average percentage of 12·7, but it included mining areas with over 30 per cent and engineering and textile districts with less than 5 per cent. It is significant that the large towns have usually much lower percentages than the smaller districts, even in the depressed counties. They offer a greater diversity of employments to their populations; the risks are spread, and workers—especially juvenile workers—who can find no opening in the older staple trades may find work in a newer expanding industry. It is in places like Jarrow, with 53½ per cent of unemployed, Bishop Auckland with 36½, Batley with 27, Wigan with 21, and similar highly specialised districts, that the effects of trade depression are most serious.

What we have to envisage, then, is a situation in which a limited number of districts are faced with an entirely unprecedented volume of unemployment. They are entirely or mainly dependent on one or two industries, and employment in these has shrunk by a quarter or a third. Moreover, in the industries on which these towns and districts are dependent, unemployment on a large scale has persisted now for three, four and even eight years. In these towns and districts there are individuals who have been without work for six months, a year, two years. We have to allow, therefore, for the *cumulative* effects as well as for the concentration of unemployment in the depressed areas.

It is not necessary to elaborate the effects of a situation such as this. There are, first of all, the ordinary effects of poverty. The extension of unemployment insurance has mitigated the extent and the intensity of these; but it has not prevented them. Something over a tenth of the insured workers known to be unemployed at any time do not, for one reason or another, receive benefit. Benefit, where it is received, is not the equivalent, and is not intended to be the equivalent, of normal earnings, to which the worker's standard of living is adjusted. Unemployment benefit is supplemented by poor relief, but this has been restricted in the case of able-bodied men, especially in the last two years. Probably the conditions which Sir Arthur Lowry and Dr. Pearse described in their report to the Minister of Health on the South Wales Coalfields[1] are fairly representative of the worst conditions:

> The diet in the households of the unemployed men comprised little beyond white bread, butter or margarine, potatoes, sugar,

[1] Cmd. 3272.

jam, tea and bacon in limited quantity. Meat was seldom eaten except in very small amounts on Sundays, very often not more than a shillingsworth for the whole family. Fresh milk was not seen by us except when supplied from a welfare clinic, the usual milk being skimmed condensed. Fresh vegetables other than potatoes were seldom eaten. . . . Apart from diet, another factor which must tend to impair the physical condition of the poorest of the population is the insufficiency of proper clothing and footwear. The existence of this deficiency is more immediately obvious than that of insufficient food. In the houses we visited we frequently found the bed-clothing and underclothing far from adequate, and the boots not enough for the school children, to say nothing of the adults and infants. . .

It seems unnecessary to say that where unemployment has been prolonged and no other resources exist unemployment benefit is not sufficient, and still less is outdoor relief, to pay the rent and provide clothing and necessaries for a household of any size after food has been paid for.

The effects of prolonged unemployment are, however, felt before conditions such as these are reached. There is the exhaustion of savings, the pawning of possessions, and the accumulation of debt, until no more can be sold and no more credit can be obtained. And the effects do not stop at the unemployed. Indirectly the shopkeepers and property-owners of a depressed area are as dependent on the local industry as the workers in it. Therefore as unemployment on a large scale persists year after year, their trade languishes and their savings disappear. House property loses its value: there are houses in Durham put up under the Addison or later Housing subsidies for which no tenants can be found, not because the population is not there, but because no one can afford the rent. If the destruction of the poor is their poverty, even more true is it that the destruction of a depressed area is its depression.

The material effects of unemployment have, I have said, been mitigated by unemployment benefit and poor relief. But the material are not the only or even the most striking effects. The officials of the Ministry of Health, from whose report I have just quoted, emphasise this:

> Every thoughtful person with whom we have talked has expressed greater concern at the destructive effect of idleness upon the character and morale of the unemployed than at the hardships involved in the scant supply of the necessaries of life. It is a common observation that work is needed rather than food or clothing. We feel that there is much justification for this view. From the first we were struck more by the aspect of depression among the unemployed men and their listlessness than by any other signs of poverty.

This listlessness must not be confused with unwillingness to work. The great mass of the unemployed realise, more acutely than any observer can, that it is work, not relief, that they need. The experience of the officials who administer the unemployment insurance system and poor relief is that, even when a succession of failures may have discouraged a man in his search for work—and he cannot have unemployment benefit unless he is "genuinely seeking employment"—he will still take any work that is offered. But skill rusts through desuetude, and a man's physical fitness for work is reduced by prolonged lack of work; so that a man has sometimes a difficulty in resuming work when the opportunity comes. This loss of industrial quality is one of the heaviest costs of post-war unemployment.

The depression of spirit which struck the Ministry of Health officials—and all other observers—can be traced to deeper roots than the loss of skill and in-

dustrial quality. There is nothing so irksome to an active man as continuous and compulsory idleness; and, if we are bored long enough, we inevitably become depressed. In the case of the unemployed in the depressed industries, this effect is reinforced by two other influences as potent. There is the feeling that their distress is undeserved, and that they can do nothing themselves to relieve it. Among the miners there is a widespread feeling that the rest of the community could have done much more than it has done to prevent their industry from reaching its present plight; that is stated merely as a fact, without any suggestion that their feeling is justified or the reverse; though active discontent and resentment of this sort is a healthier state of mind than the "depression" and "listlessness" referred to a moment ago.

It must be remembered, if we are to understand how easy it is to despair, that the industries that are most depressed now are those which were expanding most rapidly before the war; and that in these specialised districts, if the main industry declines, there is no alternative to which the population can turn. There are, of course, the generally diffused industries, such as building, engineering and transport; but these all depend on the principal local industry, and—in the depressed areas, even if they are busy elsewhere—share its depression. The result is that there are no openings to which a worker, displaced from his accustomed work, can turn, and—what is even more important—too few openings to absorb the boys and girls leaving school.

CHAPTER III

DEFLATION AND UNEMPLOYMENT

I. *The Meaning of Deflation*

THE analysis of the last chapter pointed to a general correspondence between the course of employment and the movement of prices. This correspondence is the source and justification of the common view, that post-war unemployment has been caused by the monetary policy pursued by the Government and Bank of England in co-operation; in other words, that unemployment has been due to deflation. This view does not exclude the influences of other factors, affecting particular industries, such as were suggested by the varying fortunes of different industries; but asserts the importance of monetary policy as the major general influence, affecting all or most industries, and accounting for the big general movements of industrial activity. It is necessary therefore to examine this influence.

Several questions are involved in any examination of the bearing of monetary deflation upon post-war unemployment. What exactly is meant by "deflation"? How and by what methods did the Government and Bank effect deflation? How exactly does deflation cause unemployment? Was the action of the Government and the Bank the sole and sufficient cause of the unemployment which apparently followed from

it; or, if not the sole cause, the principal cause? And finally, if the action of the Government and Bank did cause unemployment, was there a justification for that action on grounds that compensated for the inevitable cost and suffering of the incidental unemployment? These questions will now be examined in turn. The Government and the Bank of England are conjoined in the inquiry, because the monetary policy of the country has been determined by them in co-operation, and it is impossible for any layman to discover the degree of responsibility that they must respectively bear.

Deflation, for the purposes of the present inquiry, may be defined as the deliberate reduction in the price level by a restriction of the supply of money or means of payment. It is conceivable that a Government or Central Bank might initiate a policy of restricting the supply of means of payment without intending to reduce the price level; but, since such a policy would almost certainly have that result, it would come under our definition; the action would be deliberate, and its tendency would be to reduce prices, even if the reduction of prices was not its object.

There are a variety of methods by which deflation can be effected. A Government or Central Bank may curtail the number of currency notes outstanding; this is an immediate restriction of the means of payment, which involves an indirect and more important restriction, in the restriction of credit which becomes necessary when the supplies of legal tender available for the banks' cash reserves are reduced. This is the most direct and obvious method when the monetary system includes legal tender inconvertible currency notes, as the British system did in effect until 1925. The second

method is the raising of the Central Bank's rediscount rate ("Bank Rate" in England). This has the effect of making credit more expensive, and so compelling economy in its use; the money market, having to pay the Bank more for credit, will raise its charges to the businesses which depend upon it for credit in the form of advances and bills; at the higher charge they will take less, so that the means of payment represented by cheques drawn against advances and bills will be reduced in quantity. A third method, also indirect in its operation, is the sale of securities by the Central Bank. The effect of this is to transfer to the Central Bank, which will withhold it from circulation, the money which is paid for the securities, and so to reduce the supply of money available for business.

To these three methods two others must, in the special circumstances of 1918–25, be added. So long as the country had not returned to the Gold Standard, a reduction in the Government's Floating Debt, or even a check to its increase, was likely to have a deflationary effect. So long as the market held large quantities of short-term Government obligations, and the limit to the creation of cash imposed by the Gold Standard was not operative, the ordinary checks upon the expansion of bank credits, and so of means of payment, were not effective. Credit could be expanded and lead to a rise in the price level, which in turn would lead to an increased demand for legal tender currency for wages and retail trade, without the diminishing ratio of bank reserves to demand liabilities exciting anxiety and compelling a contraction of credits. The banks and other agencies could always shift on to the Government's shoulders the obligation of finding the additional cash required, by letting the Government obligations they held run

out and refraining from renewing them. The Government would then have either to print more currency notes or to borrow from the Central Bank; in the latter case the cheques it drew against such advances would come into the hands of the other banks and credit agencies, who would thereby acquire credits with the Central Bank which they could treat as cash for the purpose of strengthening their cash reserve ratio.[1] The immense Floating Debt of 1919–20 was the real basis of the inflated bank credits, which sent prices soaring in the boom of those years.

The other instrument of deflation ready to the Government's hand in this period was the removal of the embargo on the export of gold. This embargo, until it was removed in 1925, made it unnecessary to take into account, in deciding the safe limits to which credit could be expanded, the possibility of a foreign drain of gold which would deplete the country's cash reserves. Nominally currency notes were convertible on demand into gold; virtually, so long as any gold so obtained could not be exported, they were inconvertible. The country's monetary system, therefore, was independent of those of other countries. Under the Gold Standard there is an automatic check on inflation. If a country's price level rises relatively to other countries, the exchanges move against it, gold flows out, and the monetary authorities are compelled, in defence of their gold reserve, to raise the rediscount rate or take other measures to correct the divergence of price levels. Under an inconvertible paper standard a relative rise in the price level will be followed, as under the Gold Standard, by an adverse movement of the exchanges; but this will not compel deflationary measures,

[1] Cf. Cunliffe Committee's 1st Interim Report, § 11.

designed to bring the price level back into relation with other countries, if the monetary authorities do not choose to adopt such measures. They might, of course, take such measures—if they were wise, they would; but they would not be under the same compulsion to do so as they are when their ultimate reserve consists of gold, which would leave the country if they did not adopt them. The restoration of the free export of gold, therefore, would have a deflationary effect, by compelling the monetary authorities and the joint-stock banks to watch exchange movements, and to restrict credit the moment an adverse movement threatened a drain on their cash reserves.

II. *What did the Government do?*

How then did the Government and the Bank effect deflation, if the fall in prices was, in fact, the result of deliberate policy? What exactly did they do? Actually they seem to have done very little; though very little may have been needed to bring prices down. In December 1919 they expressed their approval of the Cunliffe Committee's report, in which the return to the Gold Standard at the earliest possible opportunity was laid down as the aim to which monetary policy should be directed, and accepted the committee's recommendation that the note-issue outstanding at the end of one year should be the maximum for the ensuing year. Their explicit action, therefore, was not deflationary, since it involved by itself no curtailment of means of payment; it was directed rather to checking further inflation. There is no doubt, however, that the declaration of policy had a decisive effect, since its unity and loyalty are the chief characteristics of the London

Money Market. This effect was reinforced by the financial transactions of the Government in the following year. Revenue exceeded expenditure in the first quarter of 1920, and the growth in the amount of outstanding Treasury Bills was checked; the growth was resumed after the coal stoppage at the end of the year, but by then prices had turned. The restriction on note issue, coupled with the curtailment of the Floating Debt, meant that the market could no longer rely on an expansion of the cash resources provided by Government, if credit was expanded further.

The changes in Bank Rate reinforced these considerations. It was raised from 5 to 6 per cent on November 6, 1919, and to 7 per cent on April 15, 1920. Wholesale prices reached their peak in April and began to fall in June. Thus the Government and Bank, in addition to stopping further inflation, did deliberately take steps to secure some restriction of credit. The fall in prices has been attributed to other causes, particularly to a "buyer's strike" against the existing level of prices;[1] and other factors operated to bring about a general fall, particularly the expansion of production as industry succeeded in reorganising and redirecting itself after the war.[2] But there seems no reason to doubt that, while other influences were operative, the Government and Bank's policy was deflationary and was effective in this sense. What justification there was for it will be considered later. The allegation is sometimes made that the Government's deflationary object was pursued, not by the overt measures just described,

[1] Cf. H. W. Macrosty, *Statistical Journal*, 1927, pp. 45 *et seq.*, for an exhaustive discussion of this subject.

[2] According to the Index of Production given in the London and Cambridge Economic Service Bulletins, production reached a higher level in each of the first three quarters of 1920 than in any other quarter since the war.

but by an organised restriction of credit on the part of the joint-stock banks. Actually aggregate deposits and advances showed a considerable advance in the half-year in which prices turned, and were maintained at this high level for another nine months, during which prices were falling rapidly. Nor was any "organisation" needed in the conditions of 1920 to compel banks to scrutinise applications for further advances and overhaul outstanding overdrafts.

In 1925 the Government's initiative was even more limited. When the American exchange was "unpegged" after the war, an Act was passed prohibiting the export of gold except on licence. This Act, unless renewed, expired at the end of 1925. The Government, therefore, had only to refrain from renewing this Act to bring the country back on to the Gold Standard. It was generally anticipated in the latter half of 1924 that the export prohibition would not be renewed, and the raising of the Bank Rate to 5 per cent in March 1925 was taken, correctly, as evidence of the Government's intention. The Chancellor of the Exchequer announced on April 28 that the Act would not be renewed, and that the Bank would be given a general licence to export gold at once, so that in effect the Act ceased to operate from the time of the announcement. It was announced at the same time that credits had been arranged in New York, which could be drawn upon to support the sterling-dollar exchange if necessary, until the adjustment of prices and trade which would make such artificial support unnecessary had been effected. These credits were in the event not used.

III. *Deflation and Unemployment*

Leaving for the moment the question of the Government's responsibility, let us turn to our third question—in what way deflation causes unemployment. The answer is primarily by the fall of prices involved, and incidentally by the restriction in the amount, and raising of the price, of credit, involved in bringing prices down. It must be noted that prices might fall from causes other than the monetary policy of the Government; it should be remembered also that a falling price-level, as the recent example of the United States shows, is quite consistent with industrial prosperity. If a fall in prices is brought about by a policy of deflation, however, it will almost certainly cause unemployment.

This result would not follow if all prices, including the prices of labour, capital and credit, were affected at the same time in the same degree; but this never happens. Deflation causes unemployment by bringing about a divergence between costs and selling prices, and so discouraging and depressing industry. This it does in two ways.

As we have seen, there is, in the upward and downward movement of trade, an inevitable *time lag* between the movement of expenses and the movement of selling prices. The chief elements in expenses that lag in this way are wage-rates and fixed interest charges. If wage-rates are maintained while prices fall by a third, the real cost of labour, other things remaining equal, is increased by a half; the burden of debentures or other loans raised when the price index is 200 is doubled if the price index falls to 100. The collapse of the post-war boom is only the most striking instance

of this dislocation. The extent of the fall in prices was greater than in any recent English experience—from an index number of $325\frac{1}{2}$ (1913 = 100) to 154—and the rapidity of the fall equally without modern precedent —from $325\frac{1}{2}$ in May 1920 to 202 twelve months later, and 154 by September 1922. In 1924–25 the correlation between price movements and employment was not so obvious; but an exact monthly correspondence was not to be expected. The seasonal movement of unemployment obscures any relation between the two; the trend of employment again may have been upward, so that the effect of the fall in prices was to prevent a reduction rather than cause an increase in unemployment; and the course of employment was greatly influenced, first by the fear of a stoppage in the coal-mining industry, and then by the subsidy which was given to avert a stoppage. But the movement of prices must have had its normal effects, since there was on balance no reduction in wage-rates, and the fixed charges in industry had to be met in money of increasing value. The wholesale price index, which was 162·6 when unemployment reached its minimum in June 1924 and 166·2 at the end of the year, had fallen to 155 by September 1925 and to 144 by March 1926.

The other way in which a fall in prices may cause unemployment has been of exceptional importance in the post-war period. Briefly, a fall in prices may bring about a divergence between costs and selling prices, not only in time but in space. A large part of British industry is carried on for export; another large part is subject to the competition of foreign imports in the home market. It is, therefore, affected by anything that alters the relation between the purchasing power of the pound sterling and that of other currencies.

Differences in the purchasing power of two currencies tend to be expressed in the rate at which they exchange in the foreign exchanges. Thus if £1 will buy as much as 25 francs, the exchange rate will be £1 = fr. 25. If now the purchasing power of the franc falls, so that 100 francs will buy only as much as 25 francs would buy before, the exchange rate will tend to move to £1 = fr. 100; if later the purchasing power of sterling is halved, the exchange rate will tend towards £1 = fr. 50. Now the changes in the purchasing power of a currency, as we have seen, are not uniform in relation to all commodities and services; we have seen, for example, that when prices as a whole fall, the fall is less and slower in the case of the prices of labour and capital (wage-rates and fixed interest charges) than in the case of world staples like cotton and pig-iron, and the same is true of rents, railway rates and local rates. The movement of exchange-rates, therefore, if it equates the purchasing power of the two currencies in respect of commodities entering into world trade, will not equate them in respect of labour and certain other services that enter into the costs of industry. The normal tendency of business men to buy in the cheapest market will prevent any lasting divergence between the prices of the same commodities in different currencies and the exchange rates of those currencies; if, when £1 exchanges for fr. 100, they can buy more goods with fr. 100 than with £1, they will turn their pounds into francs, and British producers will have to offer their goods at lower prices in sterling if they wish to sell their goods. But the costs of British producers may not have fallen, so that they can reduce their prices only at a loss. This is what happened in 1925 and the following years. As prices fell, the exchange

value of sterling went up; British exporters had to accept fewer pounds for their goods, but they were not able to reduce their costs proportionately, by paying fewer pounds in wages and fixed charges.

The influence of divergencies of this sort between the internal and external purchasing power of currencies has been so great since 1920 that it is worth a little more consideration. It explains the advantage in export trade conferred upon a country by a depreciating currency. The value of the currency in the exchanges falls more rapidly than its purchasing power at home. Hence purchasers in other countries, by buying its currency at its low value in the exchanges, can get its products cheap, and so will prefer them to competing products of other countries. Or, to put the same thing from the point of view of the home manufacturer or merchant, since wages and other costs have not risen so much as the prices of products entering into world trade, he can cover his costs and still sell at something under his competitors' prices in other countries; he can take less than they require in *their* currency, and still, after exchanging it into the currency *of his own country*, have a surplus over his expenses of production.

On precisely similar lines the export disadvantage of a country with an appreciating currency is explained. The British exporter, for example, in 1925 could not demand more dollars or marks for his exports than he had been getting when the British price-level was higher; but the dollars or marks he got, owing to the rise in the sterling exchange as the British currency appreciated, would not exchange for as many pounds as before. Either, therefore, he had to get his costs down in the same proportion, or accept a lower—possibly an adverse—margin between receipts and expenses; and he could

not always get his costs down, because wage-rates and fixed charges did not come down when other prices fell.

Actually this effect of currency appreciation and depreciation upon a country's competitive position is usually greater than the change in the relative purchasing power of its currency, compared with the currencies of other countries, would justify. Speculative dealings in exchange affect the value of a currency in the exchanges, especially when currencies are not tied to gold. Thus a depreciating currency will fetch less in other currencies than its true purchasing power equivalent, because speculators, expecting it to depreciate still further, will sell it forward in the hope of a profit on a further fall, and so depress its value below its purchasing power equivalent. Conversely, speculators will buy up an appreciating currency in order to make a profit by converting it back at the higher rate of exchange to which they expect it to attain, and will thus force its value above its purchasing power equivalent in other currencies. Any extensive movement, therefore, in the purchasing power of a currency is likely to impose a more than proportionate handicap or advantage on a country's export trade. Nor is it practicable to compensate for this by a continuous adjustment of internal costs to the external value of the currency. Wage-rates cannot be changed continually, nor can most fixed charges; the expense of book-keeping, not to mention the friction occasioned by continual revision of agreements and contracts, prohibit the attempt.

Apply these considerations to British industry in the years 1924 to 1926. At the beginning of 1924 sterling was apparently undervalued in relation to dollars. The United States wholesale price index

number (1913 = 100) at the end of January was 151, the United Kingdom index number 165; so far as these indications went, therefore, the purchasing power of the two currencies would have been equated by an exchange rate of £1 = \$4.45; actually the exchange rate was \$4.26. Thus it would pay holders of dollars to exchange them into pounds, at the rate of 4.26 dollars to the pound, and use the proceeds to buy British goods; and the British manufacturer, if his costs had not risen more than the rise in the general level of prices (and we have seen that they would probably have risen less), could supply these goods at a profit. Contrast the situation at the end of 1924. In December the United States wholesale price index number was 157, the United Kingdom index number 170; the rate at which, on the basis of the changes in their respective purchasing power, the two currencies should have exchanged was £1 for 4.49 dollars; actually the rate of exchange was £1 for 4.69 dollars. Whereas at the beginning of the year sterling had been undervalued in the exchanges, now it was overvalued by something like 4 per cent. It follows that it would now pay the holder of dollars to spend them in the United States, and the foreign holders of sterling to exchange their sterling for dollars or other currencies, and spend them anywhere rather than in the United Kingdom. The under-valuation at the beginning of the year was probably due to the action of speculation, which looked for a continuance of the depreciation of the British currency that had marked 1923; the over-valuation at the end of the year was due to speculators, anticipating the return to the Gold Standard in the spring of 1925, and buying up sterling in anticipation of its rise to gold parity with the dollar.

By March 1925 this over-valuation in the exchanges had almost gone, and by June completely gone; the price indices of the two countries had moved to the same level and the exchange had reached approximately mint par. Thus in the course of 1924–25 this country lost an export advantage that it possessed so long as the exchange rates did not correspond with purchasing power ratios. It followed that we had to cut our export prices if we wished to keep our export trade. Could we do this? That depends on the movement of our costs. We have to inquire, therefore, whether costs fell to the same extent as it was necessary to reduce export prices. Unfortunately there is no index of the general movement of costs; but we know that wage-rates on the average did not fall, and interest charges could be reduced only by liquidation. The average level of the prices of British exports was reduced 3½ per cent below the 1924 level by the third quarter of 1925, 7 per cent by the fourth quarter, and 14 per cent by the third quarter of 1927. A part of this —about a quarter—was made possible by reductions in the price of raw materials, such as cotton, which we import; the rest had to be effected by cheaper production, or at the expense of the exporting manufacturer's or merchant's profits.

Mr. Keynes[1] took as representative of the internal level of prices, and therefore of costs, the cost of living index number compiled by the Ministry of Labour. This he compared with the Massachusetts cost of living index number, and found that in 1924 the discount at which sterling stood in relation to the dollar was just enough to compensate the English producer for a higher internal level of prices and costs: neither country,

[1] *Economic Consequences of Mr. Churchill.*

therefore, had an advantage over the other in competing for international trade. When, however, sterling rose to par, and the cost of living in England did not fall, the English exporter was no longer compensated for his higher level of costs, and was in effect put at a ten per cent disadvantage in comparison with the American. Professor Gregory[1] made the same comparison between exchange rates and purchasing power ratios of the two currencies, but took as representative of the American internal price-level the cost of living index number of the Federal Bureau of Labour, which diverged somewhat from the Massachusetts index number. The result was to show that the exchange rates in 1924 undervalued sterling, instead of merely compensating the English producer for a higher level of internal prices, and that the rise of the sterling exchange to par merely eliminated this under-valuation, and put the English producer on a parity with the American.

The difference between these two authorities, however, does not affect the conclusion to be drawn from the changes of 1924–25. On either calculation the competitive position in world trade of the English exporter was worsened. At the 1925 rates of exchange he had to offer his goods for ten per cent fewer pounds per unit than in 1924, because it cost 10 per cent more dollars to buy a pound, and dollar prices had not risen; yet his costs, if the cost of living index number can be taken as a measure of their movement, had not come down in the same proportion.

To sum up: it would appear that before the middle of 1924 we had an advantage in export trade, due to the exchanges under-valuing our currency, and so enabling us to put goods on the world's markets at

[1] *First Year of the Gold Standard.*

prices that both met competition and covered costs. The return to the Gold Standard raised the value of our currency in the exchanges, without increasing its purchasing power proportionately over labour (and probably over other elements in costs) in the home market, and thus eliminated this advantage.

Mr. Macrosty[1] has argued that this disadvantage was temporary only; that it was attributable to speculative over-valuation of sterling in anticipation of the return to the Gold Standard; and that by the autumn of 1925 the effects of the return to the Gold Standard *by itself* had exhausted themselves. Exports were up again, and price-levels in England and America in equilibrium. He is able to show that a considerable part of the fall in the price-level, *as indicated by the wholesale price index number*, was explained by falls in the prices of important commodities, like cotton and wheat, attributable to increase in world supplies. Such falls would not harm, but assist British industry. This consideration, though important, does not, however, alter the fact that costs have never been adjusted to the lower level of prices. Unless the efficiency of labour has increased, the English manufacturer is paying higher real wages (because the same cash wages) on the average, and getting lower prices. The recovery of British exports in the autumn of 1925 may have been due in part to the operation of the Coal Subsidy.

IV. *The Extent of the Government's Responsibility*

We come thus to our fourth question—Was the action of the Government in restoring the Gold Standard, granted that it was a cause of unemployment, the chief

[1] *Statistical Journal*, 1928, pp. 303 *et seq.*

cause, and by itself a sufficient explanation, of the extent of unemployment that followed it? There are very good reasons for concluding that it was not.[1]

The circumstances of 1920 were very different from those of 1925. The boom, though fed by inflation, was due also to the intense demand for commodities, following war shortage, and the difficulty of meeting it. By the second quarter of 1920 the first intensity of this demand had been satiated, while production had increased until it exceeded the pre-war level. A collapse of prices was probably inevitable, even if the Government, by its monetary policy, had not assisted it. There is little doubt, however, that the Government's policy was deflationary, in the sense in which it had been *inflationary* before 1920, though there may be a doubt whether the succession of expedients should be dignified by the name of policy; it was in part, therefore, responsible for the depression and unemployment of 1921–22, as it had been for the feverish activity of 1919–20. In 1925 there were not the same predisposing conditions to price collapse and depression. *Prima facie* monetary policy had a greater responsibility for the change that took place.

We have seen that a fall in prices tends to bring about unemployment, and that a rise in the exchange value of a country's currency, unaccompanied by a corresponding fall in its internal level of costs, will have the same effect. The policy of 1925, then, since it both brought down prices and produced this divergence between export prices and costs, did contribute to the increase in unemployment. But there were other factors working in the same direction.

The fall in prices was not attributable solely to the

[1] Cf. Macrosty, *ibid.*

Government and Bank's action. Between January 1925 and April 1926 there was a fall of 16 per cent (from 171 to 143·6); but a large part of this was accounted for by a fall in food and raw material prices due to harvest conditions outside the United Kingdom. Another large part of the fall was due to the fall in the prices of coal, iron and steel, which again was not attributable to monetary policy, but to the renewed competition of the Ruhr. So far as the increase in unemployment was due to the fall in prices, the fall was not wholly attributable to the monetary policy of the Government. It may be noted that the subsequent fall to 138 in the present year in the level of prices, as indicated by Wholesale Price Index Numbers, can be explained by the great increase in world production of the staples of world commerce.

The fall in prices, however, is not a sufficient explanation by itself of the increased unemployment. The fall in food and raw material prices, so far from handicapping industry, would stimulate it, by making it possible to lower prices without loss and by increasing the wage-earner's margin for expenditure on things other than food. That these possibilities were not realised, the benefit of the fall in wholesale prices being intercepted by middlemen so that they were not reflected in retail prices, is not a charge against the return to the Gold Standard.

On the other hand, the depression in the heavy industries was due mainly to the resumption of Ruhr competition. The comparative activity of these industries in 1923 and the first half of 1924, though aided by the depression of the sterling exchange, was explained mainly by the interruption of German production for the European market by the occupation of

the Ruhr. The prosperity was transient and delusive, and made the subsequent employment problem of these industries more difficult, by retaining, and even drawing in, labour for which there was no permanent demand. The return to the Gold Standard at most, therefore, aggravated an unemployment problem that was inevitable, in the same way as the raising of wage-rates in the coal-mining industry in 1924 aggravated the problem.

The export industries were the industries likely to be affected most by the return to the Gold Standard. Their difficulties after the spring of 1925 were, however, largely caused, not by British monetary policy, but by renewed inflation of the currency in France, Belgium and Italy. These countries thereby secured a temporary export advantage similar to that they had enjoyed in 1921–22, and similar to that England had enjoyed over America in 1923–24. This was a development entirely outside the control—or even anticipation—of the English monetary authorities, which would have caused unemployment in the English export industries if the Gold Standard had not been restored, unless the English currency had been inflated simultaneously and equally.

Finally, when these important continental competitors stabilised their currencies, they did so by devaluing their unit of account, so that little deflation was necessary. The level of wholesale prices at which France stabilised (pre-war = 100) was about 620, Belgium 850, Italy 460. The advantage, therefore, which their industrialists had gained from inflation, in lowered real wages, a reduction of the true burden of loan and other fixed charges, was preserved for them. In England, on the other hand, wage-rates and the full

burden of interest charges have been maintained, while export prices have been reduced by 14 per cent. Even with all these disadvantages, it is not clear that British industry might not have recovered and met the strain of the restored Gold Standard, if the national lock-out in the coal-mining industry had not intervened.

To sum up: deflation was a cause of unemployment, but not the sole cause. It was a cause, because the immediate effect of the return to the Gold Standard was to handicap the export trades by compelling them to accept lower prices, corresponding with the rise in the exchange value of sterling, while internal costs remained on their previous level. It was reasonable at the time to anticipate that this handicap would be temporary only, the internal price level falling and competitors' prices rising; but in fact it has persisted. Partly this is due to the rigidity of wage-rates, which remain on an average at the 1924 level in spite of an 8 per cent fall in the cost of living, while export prices have fallen 14 per cent; partly to the heavy burden of indebtedness incurred by industry and the State, the charges on which are not reduced when other prices fall; but mainly to the subsequent inflation, and stabilisation at a high price-level, of the currencies of our chief continental competitors. The increase in unemployment was also due in part to the resumption of German competition in the heavy industries. Although Bank Rate was raised, credit supplies were not restricted, aggregate bank deposits amounting to £1647 million by the end of 1925, when the wholesale price index had fallen to 152, as compared with £1656 million at the end of 1924, when the price index was 180.

The last question we put ourselves—Was the Government's action justified on other grounds, even if it caused unemployment?—is not strictly relevant to an inquiry into the causes of unemployment, and in any case has been answered by implication. Even the critics of the Government's action in 1925 admit that there was a case for deflation in 1920. We have seen that the Government's action was confined to accepting the Cunliffe Committee's recommendations and simultaneously attacking the Floating Debt, while the Bank attacked inflation more directly by raising the Bank Rate. The reduction of the Floating Debt was overdue; the criticism to which the Government was really open was that, by reducing taxation in 1919, it had permitted the debt to reach dangerous dimensions. Since the Floating Debt was the real basis of inflated credit, its reduction was certain to lead to deflation, although deflation was in no way the object of the reduction. It may be argued that there was no need to precipitate a fall in prices by restricting the note issue and raising Bank Rate. On the other hand, the prosperity which inflation had brought with it was due not to the *high* level, but to the *rising* level of prices; and, to maintain it, it would have been necessary to force prices ever higher. To defer the measures the Government took, therefore, would have been to run the risk of launching the country down the slippery slope that Austria, Germany, France and Belgium all took. Ultimately a restoration of the currency would have been inevitable, and, painful as it was, it was probably less painful in 1920 than it would have been had inflation been allowed to proceed further. Unfortunately the process of restoring the Gold Standard was not completed—perhaps in the disturbed con-

ditions of the world it could not be completed. Prices were allowed to rise again, and the sterling exchange against gold to fall. Consequently a second attack was necessary; this was made in 1925.

The Government's action in 1925 was confined to the negative policy of not renewing the gold export prohibition. Bank Rate was raised to 5 per cent, but nothing else proved necessary. Now, to have renewed the gold export prohibition then would have been to set back the whole movement for restoring the world's currencies to a common gold basis, and, therefore, deferred perhaps for another decade the restoration of the same stability in the exchanges as existed before the war. South Africa, Holland and Germany were all back, or going back, to the Gold Standard, whether England followed suit or not; so that the circumstances were favourable to an attempt to restore the Gold Standard generally. Moreover, a chance was offered by the easy credit conditions of New York,[1] and subsequent rise in American prices towards the English level. The Government in their decision merely took a chance which America offered. It involved a handicap to British export trade; but in the long run England stood to gain more than any other country from the elimination from trade of the uncertain element of fluctuating exchanges. The real justification of the decision is to be seen now in the comparative stability of the European currencies, almost all of which are once again tied to the common measure of gold.

Moreover, if the chance of contributing to the restoration of the world's Gold Standard had been let slip, the results for British industry might have

[1] The New York Federal Reserve Bank rediscount rate was reduced to 3 per cent in August 1924.

been not less damaging. Immediately, the extension of the gold export prohibition would have led to bear speculation in sterling and the withdrawal of foreign balances from London. In order to prevent a further depreciation of sterling it would have been necessary to restrict credit and raise discount rates, which might have handicapped industry as seriously as the rise in sterling exchange. In the long run the continued dislocation and uncertainty which fluctuating exchanges involved would have cost the export industries as much as they were forced to sacrifice in order to get the exchanges back on a gold basis.

Deflation, it is fair to conclude, was inevitable; certainly it is not fair to attribute to it all the unemployment that the country has suffered from since 1925. The resumption of German competition in the heavy industries, and the intensification of French and Belgian competition under the stimulus of further inflation, were equally important influences. Moreover, unemployment in 1924 amounted to over a million persons, and on more than one occasion since the return to the Gold Standard a lower rate of unemployment has been reached. Deflation, therefore, by itself will not explain the post-war unemployment. It is one influence, perhaps the most important single influence of a general character; but there are other influences that have still to be examined. The influence of deflation persists, because it is not yet complete. Debts, wage-rates, Government charges, are all still on the basis of 1924 prices, before the final step in the restoration of prices to a gold basis was undertaken, if not of earlier, higher levels. Their burden could be lightened by renewed inflation; but the restoration of the free export of gold makes such a policy no longer practicable.

CHAPTER IV

THE EXPORT INDUSTRIES

I. *The Concentration of Unemployment*

We have seen that no single influence would explain post-war unemployment. After all allowance has been made for the influence of deflation, there remains a residuum of persistent unemployment that deflation intensified and that inflation might conceivably remove, but that deflation did not cause. The divergent and contrasting fortunes of different industries, which all nevertheless account for an important fraction of the persistent unemployment, point to the conclusion that the problem is not a simple phenomenon, attributable to a single cause, but a bundle of problems, each explained by a different set of causes.

It is not possible to follow out the recent history and present position of all the industries in which unemployment since the war has been severe. Nor is it necessary; for the Balfour Committee has made such a survey. It may be possible, however, and the attempt is worth making, to distinguish the chief types of influence that to a greater or less extent have determined the course of employment in all the industries in the depressed group, to group under two or three heads all the factors that explain the persistence of unemployment represented by three-quarters of a

million unemployed in excess of the number that ordinary trade fluctuation would account for.

The clue to such an explanation is the percentage distribution of the unemployed at different dates, given above in Table II., p. 39. The table brings out the concentration of unemployment in a limited group of industries, and the change in the contribution that each has made. It is not necessary to spend long over two of the industries selected. Building has been in the past, and is at present, an important contributor to unemployment, but its unemployment is due to causes peculiar to the industry. There is, first, an excessive number of labourers in relation to the skilled men available, with the result that, even when the industry was at its busiest in 1927, it still had a large number of unemployed. In the second place, the fluctuations in its activity are explained almost entirely by the Government's housing subsidies. The Addison scheme led to intense activity, which was succeeded by equal depression when that scheme was cut short in the interests of economy. The grant of a new (the Chamberlain) subsidy in 1923 led to a revival, accentuated by the Wheatley subsidies of the following year, and checked after 1927 by the reduction and termination of subsidies.

The other case which calls for a special explanation is the dock industry. Here unemployment has no doubt been influenced by the decline in the physical volume of foreign trade; but, apart from this, there is nothing new in the situation. Unemployment is due to the excessive number of persons dependent on the industry at the best of times, drawn to it and trapped in it by the system of casual employment.

Apart from these two industries the main contri-

butors to the mass of unemployment have been as follows: in the earlier periods, the metal, shipbuilding and engineering group, in the later period coal, and intermittently, without much relation to the other two, the great textile industries. It will be noticed that these comprise the staple industries of pre-war Britain; the other characteristic they have in common is that they are all very dependent on export markets. So far as can be estimated from a comparison of total output, as measured by the Census of Production in 1924, and exports, coal was dependent on overseas markets for the disposal of a fifth of its product, shipbuilding about a half, engineering a quarter, cotton probably four-fifths, woollen and worsted over half, iron and steel a third. Where the proportion was least—in the case of coal—the dependence was as great as in any of the other cases, since domestic consumption of coal has been maintained, and it is the loss of export trade that has caused depression and unemployment.

The proportion in which the members of this export group have contributed to the total of unemployment have varied from year to year; but, as Table II. shows, their aggregate contribution has always been substantial, and excessive in relation to the proportion of the total occupied population engaged in them.

It will be remembered that our examination of deflation showed that the return to the Gold Standard would be likely to affect most just this group of industries. We can distinguish three general influences, or collections of influences, that explain the exceptional depression of the group—the effect of the war in expanding industries beyond normal peace-time requirements, the effect of the war in stopping the adjustment to changing competitive conditions, and the

differential burden of costs, as compared both with other British industries and with foreign competitors, for which deflation accounts in part, but only in part.

II. *Over-Expansion in Munitions Industries*

The expansion of all industries from which munitions supplies were drawn is the chief explanation of the preponderance in the earlier years of depression of the metal and engineering group. The real rate of expansion can be realised only by contrast both with the pre-war decade and with the contemporary expansion or decline of other industries. Exact figures are not available, because an occupational census is available only at ten-yearly intervals; but the following Table (IV.) sufficiently indicates the changes that took place during the war:

TABLE IV

TRENDS OF EMPLOYMENT, 1901–1921

Increase (+) or decrease (–) : per cent

	1911–1921.	1901–1911.
Occupied population of Great Britain	+5	+13
Metals, machines, conveyances	+40	+22
Chemicals	+47	+47
Coal	+16	+36
Cotton	– 5	+11
Wool	– 4	+14

If actual numbers instead of percentages be considered, the expansion of the munitions industries is even more remarkable, The total occupied population increased from 18,354,000 to 19,357,000 between 1911 and 1921, an increase of 1,003,000. Nearly three-quarters of this, 712,000, was in the metal, machines,

conveyances group, which increased from 1,779,000 to 2,491,000. Even more striking are the figures for males only; the number of occupied males in Great Britain as a whole increased by 726,000; of these 581,000, or 80 per cent, were in the metals and engineering group. In the other industries, including coal, there was probably some expansion between 1911 and 1914 and again in 1919 and 1920, which must be allowed for in estimating the changes in the war period itself. In the munitions industries also, there was expansion after the Armistice in spite of the cessation of munitions demand;[1] Sir Hugh Bell has stated that the new equipment installed in steel-works under pressure of the Government was not used before the war ended, so that the additional capacity of the industry was available only after the war. The effect of these additions to equipment upon the post-war fortunes of these inflated industries is enhanced by two considerations; the equipment was installed at a very high level of costs and largely financed by loans and debentures, on which a fixed rate of interest has been due ever since; and the expansion was not confined to this country, every other belligerent and most neutrals having simultaneously expanded their productive capacity.

An expansion of this character, to meet a transient and abnormal demand, must inevitably be followed by unemployment, if no new peace-time demand could be discovered to take the place of the demand for munitions. In time it may be expected that the world's demand will grow up to its expanded productive capacity; pending such a growth, unemployment can be relieved only by a redistribution into other

[1] Cf. *Third Winter of Unemployment*, by Astor, Layton, Clay, and others.

industries, for the products of which a demand exists, of the labour in the industry, and a check to recruiting of new labour, and by a liquidation of the capital charges incurred in the period of inflation. Such a redistribution of labour has taken place, and explains almost the whole improvement in the employment figures of the group. In the engineering group of industries, for example, the unemployed percentage fell from 17·6 in June 1923 to 8·8 in June 1928; but the actual number of persons in employment was practically the same, 845,000, as compared with 843,000. Owing to the change in the classification used in the unemployment returns, it is not possible to carry an exact comparison further back; but it is certain that there had been already a considerable efflux of labour from the group by June 1923. Between 1921 and 1927 the proportion of the insured population dependent on the engineering group of industries fell from 10·2 per cent to 7·7 per cent, shipbuilding 2·8 per cent to 1·8 per cent, and the whole metal, engineering and vehicle group from 19·2 per cent to 17·6 per cent.

The corresponding liquidation of capital is exemplified by the writing down of the ordinary shares of one of the great armament firms to one-third of their value, the drastic financial reorganisation of the other, and the less striking, but in the aggregate even more important, writing down of assets and capital in the large iron and steel firms. By contrast the example of the explosives industry is significant. Faced with a similar cessation of an abnormal demand which it had been expanded to meet, it met the situation by an organised liquidation of surplus capacity, and a collective attempt to find new outlets. Even this did not suffice to prevent a contraction in the numbers to whom the

industry gave employment; but the employment was secure, because it was not given at a loss.

III. *Check to Normal Adjustment*

The contrast between these war-inflated industries and the other industries in our table, which expanded little or even contracted in the war decade, brings us to our second head—the check to normal adjustment.

The conditions of modern industry are never static. Every industry is constantly, to a greater or less extent, changing the direction of its activities into new products, new markets, new processes; or, if it is unable to find new outlets, adjusting itself to a declining demand by a gradual restriction of enterprise. In this way the country's industries before the war were able to adjust themselves, without any apparent secular increase in unemployment, to the new competitive conditions with which they were faced by the growth of modern manufacturing industry in other countries. It would even be possible for an industry to decline and die out altogether without causing any unemployment, provided that the declining demand for its products could be met, not by turning off labour already engaged, but by stopping all entry of new labour into the industry, a process that would be completed inside a generation. This adaptability to new conditions is the chief mark and test of an advanced industrial organisation, and was certainly possessed by British industry before the war.

The cotton industry is the best example both of this pre-war adaptability and of the serious consequences that followed from the check imposed by the war upon normal adjustment to changing competitive conditions.

Foreign competition is not a new condition for the industry to meet, and the *rate* of expansion of the foreign industries, which have proved the most serious competitors since the war, was as great in the twenty years before the war as it has been in the ten years since.[1] Yet the Lancashire industry continued to expand, affording regular employment and earning modest profits. This was possible because it was never faced with any sudden or extensive change in the competitive position; the change from one year to another was always slight, and the industry was able, by finding new markets, new varieties, or new economies, to adjust itself to the new situation. Added to this, world consumption of cotton manufactures was growing, so that the growing competition was for an expanding market.

The war stopped this process of continuous adjustment, and the boom deferred for another two or three years any attempt to face the change in the competitive situation. For six years the movement of prices and costs was such that it was easy to secure a profit, irrespective of economy. There was no need to seek out new customers, when an obvious and clamant demand could not be satisfied. It is possible that the profit margins of this period have had an influence throughout the subsequent depression by accustoming manufactures and merchants to standards, for which they have been inclined to hold out when there was no prospect of securing them. In another way it has persisted, since the profits based on these margins were in many cases capitalised, the mills sold at the inflated figure so reached, and a large part of the purchase price raised by loans, the interest on which has still to be paid.[2]

At the same time the war and post-war shortage of

[1] Cf. Daniels and Jewkes, *Statistical Journal*, 1928, p. 165. [2] *Ibid.*

goods, by interrupting pre-existing trade relations, compelled many users of Lancashire textiles to turn elsewhere for supplies, or to start or develop textile industries in their own territory. It has been estimated that before the war this country supplied more than 70 per cent of the total world's export trade in cotton manufactures. This meant that there must have been markets—and important markets—which did not know, at any rate by actual experience, that it was possible to get cotton goods from any place except Manchester. During the war and post-war boom they were forced to get them from other sources, and found, not only that they could get them, but that they could get them cheaper, if not better. Lancashire still does half the world's export trade in cotton manufactures; but the diminished proportion of a diminished aggregate leaves her with a third of her capacity unused. Now, if there had been no war, the growth of competitive industries, especially behind tariffs, would still have taken place; but it might have been slower, the competition of Lancashire serving as a brake; and it need have been no more disastrous to Lancashire than the similar growth of the fifty years before the war. The English merchants and manufacturers would have adjusted themselves to it, so far as they could not kill it, by transferring a greater proportion of their production to specialities which other countries could not produce, by breaking new ground in markets which other countries had not the same facilities for supplying, and, if necessary, by a gradual curtailment of the scale of operations. Thanks to the war, ten years of such adjustment fell to be carried through all at once, and the industry has hardly begun seven years later to carry them through.

The coal industry suffered from the war in the same way, though the details of its misfortunes are different. Before the war the industry grew, less by the expansion of existing collieries than by the opening up of new collieries and new coal-fields, often by the same firms as operated the older units. The result was that the average technical equipment of the industry was constantly being raised, the new units being larger and incorporating the latest inventions. The war—and in this case too the post-war boom prolonged the unfortunate influence of the war—gave a new lease of life, because it offered easy profits on full production at remunerative prices to hundreds of old and declining pits that but for the war would have had to close. It has been necessary to close them since, but only after their struggle to survive has made the industry unprofitable even for technically up-to-date and efficient units. These old pits were able to continue producing because the opening of new pits was stopped; the average efficiency of the industry was probably reduced. Costs were further increased in the boom by the raising of wage-rates and the reduction of hours, with the result that recovery was hampered and delayed in the depression by the two national lock-outs, by which the mine-owners forced down wage-rates and lengthened hours again.

The scarcity and high cost of coal had a less obvious, but in the event even more important influence, in concealing and encouraging the growth of competition. It concealed it, by maintaining profits which in more normal times competition would have reduced, and so diverting attention from the need of measures to meet competition; it encouraged it, by compelling former customers to exploit every possible alternative to

British coal. The result was an expansion of competing supplies, the exploitation of brown coal and the rapid extension of hydro-electric schemes, the use of oil and every kind of fuel-economy device. In retrospect it would seem that the British coal industry had probably reached its apex in 1913; fuel economy and the use of alternative sources of power would in any case have checked further growth, and possibly required some contraction. The misfortune of the industry is that it had to face the results of eight years of crowded development elsewhere all at once.

If the coal industry has been as slow as the cotton industry to realise that it has to adjust itself to a changed world, it has slightly more excuse. For the necessity to face the change was postponed by the temporary interruption of German competition by Germany's difficulties between 1922 and 1924. As we have seen, the dislocation of German economic conditions by the last stages of inflation and by the French and Belgian occupation of the Ruhr was reflected in a temporary and misleading activity of English industry. The coal industry drew in additional labour, and was still able to employ a much larger proportion of its personnel than the average of industry. Profits were restored and wage-rates raised. So soon as German competition became effective again, the bottom dropped out of the market; and, except when congestion was relieved by a stoppage somewhere, the coal industry throughout Europe has been depressed and unprofitable since. The longer the task of adjusting the industry to the new competitive conditions, that grew up between 1914 and 1920, was deferred, the more difficult it became. The temporary prosperity of 1923–1924 was dearly bought at the price of concealing from

the industry the real and permanent facts of its post-war position.

All the export industries have been effected, more or less, by this six years' interruption of the normal piecemeal and day-to-day adjustment to changing conditions. This influence of the war should perhaps be regarded merely as a special case of the effect the war had in aggravating the ordinary effects of trade fluctuations. The worst effect of any boom is that it diverts attention from economies in production and reduction of costs, by making profit-making easy out of rising prices and full-time working. Then, when the boom ends, the industry is left with costs at a level which it is impossible to cover at the lower prices at which alone output can be sold. But the ease with which during the war anything could be sold, and the continual rise in prices due to inflationary finance, enhanced this normal effect. Markets were lost, or, if not lost, invaded, methods were not overhauled, labour costs were allowed to mount, and overhead expenses to expand without thought of economy; then, suddenly, in 1920 and 1921, the work of adjusting costs and methods to conditions that had been changing rapidly for six years had all to be undertaken at once.

IV. *Dislocation of Export Trade*

The greater comparative depression of the export industries has been one of the most striking features of the post-war period. It persists still, ten years after the conclusion of peace, in spite of the redistribution of much of the surplus labour drawn into the munitions industries and the partial liquidation by financial reconstruction or bankruptcy of the handicap of

indebtedness with which the boom left so many firms saddled. It is evidenced, not only by the unemployment figures, but also by the statistics of expanding and contracting industries with which the unemployment insurance scheme furnishes us annually, and by the lower level of wage-rates (compared with pre-war rates) ruling in these as contrasted with the "sheltered" industries. A large mass of unemployment persists in spite of reductions in wages greater than the average and the transfer of large numbers of workers to other industries.[1] At the end of March 1929, while the unemployment percentage for all insured industry was 10·1, for coal it was 13·2, iron and steel 16, shipbuilding 24·6, general engineering 9·1, cotton 11·5, and woollen and worsted 11·2. These six industries, comprising 25 per cent of the insured population, provided 32 per cent of the unemployed. High wages go with low unemployment, low wages with high unemployment.

The influences we have already considered explain this condition in part; but the stimulus of war demand, though concentrated on the export industries, was not confined to them. Similarly the check to adjustment, which did so much to throw the organisation of the export industries out of relation to their needs, operated equally on sheltered industries like building. Some influence that operates specifically and exclusively upon the export industries is needed to explain their plight.

One such cause was the dislocation of foreign markets and foreign trade caused by the war and the

[1] Cf. *Problem of Industrial Relations*, by Henry Clay, Ch. iii-vi, and table on p. 108. Mr. Rowe, *Wages in Practice and Theory*, throws doubt on the contrast between wages in sheltered and unsheltered industries. But the "true" wage-rates he himself calculates average 107 per cent advance on pre-war in the sheltered trades as compared with 78 in the unsheltered.

post-war settlement. There was the destruction of life and wealth, which reduced the consuming capacity of all the belligerents, but most of all the Continent of Europe, and, by impoverishing them, indirectly impoverished the extra-European countries that normally supplied their wants. Great as was this loss, it was less, in the opinion of the International Economic Conference of 1926, than the loss due not to destruction but to dislocation. New frontiers set up new tariff barriers; the credit basis of trade was weakened, and in some countries for a time destroyed; currency inflation destroyed the stability of exchange rates and introduced a new incalculable factor into all international economic transactions; exchange dumping—the sale of exports, below the cost at which they could normally be produced, by countries in which the currency was depreciating and real wages and fixed costs falling—undermined industry in countries with more stable currencies. These were adequate reasons for the exceptional depression of the export industries between 1920 and 1926.

Since 1926, however, these influences have operated with much diminished force, and yet the depression has persisted. World production, according to the indices that the International Economic Conference of 1926 was able to construct, had recovered, and passed the pre-war level by 1923, production in Europe had reached pre-war level by 1925; so that the consuming capacity of export markets as a whole by that date at latest had been restored. The worst of the other conditions obstructive of export trade have also been remedied. The currencies of all the important commercial countries had been stabilised by the end of 1926, and with the currencies the exchanges. If British

export industry did not recover its pre-war volume—and less than the pre-war volume would suffice, with reduced numbers and reduced hours, to give full employment—it must be that it was losing ground to competitors in other countries. This would seem to have been the case. The recovery, which was marked to 1924, has not been maintained. The improvement (mainly by reduction of numbers) in the metal and engineering industries has been cancelled by the contraction of employment in coal, and the other great export industries have at best maintained the position reached in 1924. Their plight can be explained only by a decline in the ability of British industry to compete, or, in other words, by a level of costs that is excessive in relation to world prices. The sheltered industries have escaped an equal depression, not because they have been able to reduce their costs, but because their prices are sheltered; the export industries must contract, if they cannot produce at world prices.

We have seen how this divergence of costs and prices necessarily followed from deflation. When prices fell, exchange rates rose; and, since it was not possible to make a foreigner give more dollars, francs or marks, the British exporter had to be content with fewer pounds per unit of export. But prices do not move all together when deflation takes place, and the prices that enter most into industrial costs are the most difficult to adjust to a general decline. Thus the exporter has been left with his prices reduced 12 per cent[1] since

[1] The average reduction in the prices of export of United Kingdom produce between the last quarter of 1924 and the last quarter of 1928 was $14\frac{1}{2}$ per cent. But the reduction in the prices of exported cotton manufactures, attributable to the fall in price of imported raw cotton, would have by itself reduced the average of all exports prices by $2\frac{5}{8}$ per cent. Cotton appears to be the only imported raw material which has materially affected the price-level of British exports; raw wool prices rose. Hence the figure in the text.

1924, and his costs at the old level. Some of these costs, and the relation of British costs and prices to those of other countries, may be looked at in more detail.

v. *Costs in the Export Industries*

The most important single cost is labour. Wage-rates are not necessarily an exact index of labour-cost, but there is no reason to suppose that British labour has become significantly more efficient since 1924, and that wage-rates are likely to be seriously misleading. On the whole wage-rates have been maintained at the 1924 level, although in certain export trades, particularly coal and iron and steel, there have been reductions; in these, however, the reduction in selling prices since 1924 is also very much greater than the average of all industry. By comparison with the pre-war period wage-rates are high, having been maintained since 1923, with the exceptions just noted, while prices generally have fallen. The cost of labour has probably been enhanced also by a reduction in normal hours, averaging 13 per cent, since 1914, which involves either extra payment for overtime or diminished use of capital equipment, and which has not yet probably been compensated by a corresponding increase in efficiency.

An important increase in costs associated with labour is the greatly increased extent and scale of insurance contributions and local rates. Before the war, in the minority of industries which came within both the National Health Insurance Scheme and the State Unemployment Insurance Scheme, the employer's contribution in respect of each workman employed was 5½d. a week or, say, 22s. 6d. a year; to-day it is 1s. 5d.

a week or 72s. a year. A part of the increase is due to the change in the value of money, which would account for an increase to 29s. 6d. a year; part to the extension of the benefits to include dependents' allowances in the case of unemployment, widows' pensions, and old-age pensions, under certain conditions, at sixty-five; part to the placing of the cost of maintaining the unemployed upon the Unemployment Insurance Fund, which is financed mainly by contributions from employers and employed. This *increase* in the tax on employment—for that is what incidentally it is—amounts to £20,000,000 in respect of insured industry as a whole, and nearly £8,000,000 in respect of the six export industries we have considered separately. It has been increased in nominal amount since prices began to fall in 1920, when a reduction might have been expected corresponding with the general reduction in prices and cost of living; an increase was even announced in the same Budget Speech of 1925 as announced the return to the Gold Standard with its inevitably depressing effect upon export prices. The real increase since 1920, when account is taken of the change in the value of money, is more than equivalent to the whole of the benefit which it is estimated that the de-rating scheme of 1929 will confer upon industry.[1]

This considerable addition to wages, represented by the employer's compulsory contributions under the State insurance schemes, has never, so far as I have been able to ascertain, been taken into account in fixing wage-rates. It is nevertheless an addition both to the real income of the wage-earners and to the

[1] Employer's contributions in 1920, 9d. per week per man, the equivalent of 4d. to-day.

labour costs of the employers. Local rates, until they are reduced by the de-rating scheme, are similarly a burden, the weight of which has increased since the war and since 1924. They constitute a burden in the same way, because they have to be paid whether the industry is working at a profit or a loss, and the burden has increased for much the same reasons; partly because money has fallen in value, partly because new duties and charges have been imposed upon local authorities, partly because provision for unemployment, so far as it is not made by the insurance scheme, is left to the Poor Law. Hence the burden is heaviest where a locality is dependent on a single industry and that industry is depressed.

Another cost, the burden of which has been materially increased by the change in the value of money, is the burden of loan and debenture interest. In the prosperous years 1919 and 1920 many firms issued debentures, or incurred other forms of indebtedness, in order to finance extensions and reorganisations called for in turning their activities from a war-demand to a peace-demand, or merely to finance purchases of raw materials and other requirements at the high level of prices then ruling. They found themselves left, when prices fell, with these obligations, on which interest had to be paid in money that had doubled in value. The £30 millions of debt, with which the Lancashire American Cotton Spinning industry saddled itself, was incurred on the average in pounds that were equivalent to eight shillings each in pre-war money; they have had to be paid back, or interest on them met, in pounds equivalent to fourteen shillings in pre-war money. The sheltered industries can adjust their prices to cover such charges; the industries engaged in export, or

exposed to foreign competition in the home market, have to sell at prices set by this competition, so that even when they make a trading profit their profits are related to the present level of prices and will not always suffice to cover charges still on the level of 1920 prices. Slowly and painfully the burden is being liquidated, by the bankruptcy of the more heavily indebted firms and by writing down of capital in cases where the firm survives; but the process is very far from complete, and all debts and charges incurred after 1915 will have to be written down or written off before the competitive position of these industries will have been restored under this head alone.

Much greater in the aggregate than the whole of the indebtedness incurred by industry in the period of high prices is the burden of the National War Debt; but the effect of this upon costs is indirect. The service of it is met by direct taxation, which is not paid by firms that are making no profits and is not, therefore, a cost to industry. But indirectly it is a serious handicap, since the direct taxation to which it gives rise trenches deeply into the profits available for expansion and re-equipment. The need of such capital resources for re-equipment and reorganisation is probably greater than at any pre-war period, and the funds from which they may be drawn are smaller; yet they are further reduced by Income-Tax, Super-Tax, and Estate Duties, probably by a third at least. The rise in prices to 1920 reduced the real weight of this handicap; the subsequent fall in prices increased it. Its weight was increased again by the further fall in prices since the beginning of 1925.

A comparison with the course of prices in other countries is needed to bring out the handicap under

which these costs place the British export industries. At the end of 1928, when the British wholesale price index number was about at the level of the latter part of 1915, the United States price level was about the same as that of 1917; Belgian prices were stabilised (with British assistance) about their peak; French prices were lower than in 1926, but still higher than in 1920; Italy's price level about that of 1918–19; while Holland alone had brought prices down to the comparative level to which English prices had been brought. Germany and Austria had virtually extinguished internal debts before stabilising. In every case, therefore, except that of Holland, some of the gains of inflation, in reducing the burden of industrial and public indebtedness, had been retained, while in the case of the most serious competitors of British industry —France, Belgium, and Germany—almost the whole gain had been retained. Wages and other costs, though not fixed in terms of money like debt-charges, are nevertheless reduced by inflation; so that these also would give continental competitors an advantage over British industry. In discussing the effects of deflation we had occasion to cite a method, used by Mr. Keynes and Professor Gregory, for measuring the effects of changes in the price level upon costs and competitive advantages. The cost of living index number is taken as representative of the internal purchasing power of a country's currency and therefore of its costs. If, then, one country's index number has risen more or fallen less than that of another, and the advantage is not cancelled by a corresponding depreciation in the first country's exchange, it should have a competitive advantage over the other in foreign trade. It was shown by this method that in the year 1924–25, in

which England returned to the Gold Standard, British export industries lost a 10 per cent advantage (or were put at a 10 per cent disadvantage) by comparison with America's industries. Applying the same method to a comparison of England with France, it appears that between 1914 and 1927 English industry was placed at a 40 per cent disadvantage in competition with French industry.[1]

In this connexion another effect of inflation upon competitive efficiency may be referred to. During the period of inflation in Germany the directors of industry made large profits at the expense of their fellow-countrymen, whose incomes did not rise proportionately. These profits they were unwilling to retain as bank-deposits or in other liquid form, because the further rise in prices would have reduced their real value; they used them, therefore, to extend and re-equip their plants, with the result that German industry ended the period of inflation, short indeed of liquid

[1]

	Cost of Living Index Number.		Exchange Rate.
	England.	Paris.	
1914	100	100	£1 = 25.15 fr.
1924	171	366	£1 = 87 fr.
1927	164	525	£1 = 124 fr.

The calculation may be put this way, the assumptions being that costs in the two countries were in equilibrium with the exchange rate in 1914, and that the cost of living index numbers may be taken as representative of the subsequent movement of costs. In 1914 goods which cost £100 to produce in England, cost fr. 2515 to produce in France. In 1927 the same goods would cost £164 to produce in England (£100 × $\frac{164}{100}$), and fr. 13203 (fr. 2515 × $\frac{525}{100}$) in France. At the rate of exchange ruling in 1927, however, the French producer would cover his costs, if he obtained £106·4 (fr. 13203 ÷ 124) for the goods. He could therefore afford to undersell the English producer by £57·6 (£164 − £106·4).

capital, but with extensive modern plants on which there were no debt obligations. In France and Belgium a similar modernisation of plants was made possible, partly by the profits of inflation, partly by the disbursements of the Government in compensation for destruction of plant during the war. The chief continental competitors of British industry have, therefore, an important competitive advantage in more modern equipment and, in some industries, a larger scale of enterprise.

To sum up this chapter: the post-war problem of unemployment is primarily a problem of the older and greater export industries. These were adversely affected by the war in three chief ways: by an uneconomic expansion induced by the demand for munitions; by the check to the normal process of adjustment to changing competitive conditions imposed by the war and post-war boom; and by the deflation of the prices they receive, without a corresponding reduction in the costs they have to pay, at a time when their chief competitors had their costs reduced by inflation. These industries have done much to restore their former activity, by redistribution of labour, writing down and writing off of capital, and reduction of wages; but not enough to restore their pre-war competitive position. They have as a group made the greatest sacrifices in order to overcome the disturbance of normal economic activity caused by the war, but are still the chief sufferers. Their losses are as directly and certainly a cost of the war as the losses which are represented by the War Debt or War Pensions, but they have not received the same recognition.

CHAPTER V

RECENT POLICY AND ITS IMPLICATIONS

I. *The Alleged Recovery of Industry in 1929*

UNTIL unemployment became an issue in a General Election, no one questioned the existence of a problem. Even when party-political exigencies began to influence statistical argument, the difference that emerged was rather between those who regarded unemployment as so severe that highly novel and unprecedented measures were justified, and those who saw steady improvement, which rendered undesirable the risks attendant on any novel experiment, than between a party that affirmed and a party that denied the existence of a problem. There was, however, explicit or implicit in the arguments put forward by opponents of special measures, the view that unaided private enterprise, or private enterprise aided only by measures already available and by the natural expansion of new industries, would ultimately solve the problem; and for this view the authority of the Industrial Transfer Board, whose report was the first official inquiry to insist that the problem was not a transient effect of ordinary trade fluctuation, might be claimed.[1] It is necessary to examine the diagnosis that

[1] Cf. the following extracts from the summary of conclusions: "Transfer must be so far as possible a natural process and lead to permanent absorption.

leads to this policy of *laissez faire*, and to begin with the recent figures of unemployment.

The first four months of 1928, judged by the standard of the unemployment insurance figures, were better than the corresponding months of the previous year and of any year since 1921; unemployment then became worse, the percentage for each of the last six months being higher than the average for the corresponding months in the years 1922–25 and 1927. By the end of January 1929 the number of recorded unemployed was 1,466,000. From January onwards the figures improved; by the end of March the number had fallen to 1,204,000, by the end of April to 1,181,000. This improvement was, however, mainly seasonal, a reduction by 200,000 being due on account of seasonal influences alone.[1] The improvement was influenced also by the weather, which affected building and contracting, in which the number of recorded unemployed fell by 90,000, and probably by the continuing influence of the dispute in the German metal industry in the previous autumn. The best test of improvement, however, is the relation between the increase in the number of insured persons and the increase of the number actually in employment. Comparing the first

Within this country it must ultimately rest upon natural economic development. . . . The elasticity of the employment market makes practicable the absorption in ordinary industry of a large part of the surplus without permanent prejudice to other workers. . . . If action on the lines of our report be taken promptly and pressed resolutely, the problem, grave and stubborn though it is, will not be found incapable of solution. . . . Only by concerted movement alike within our shores and within the Empire can the desired objective be attained" (*Report of the Industrial Transference Board*, pp. 55-56).

[1] *I.e.* measuring the effect of seasonal influence by taking the average deviation of each month for the years 1922–25 and 1927 from the trend of the unemployment percentages. The average reduction in the four preceding years had been 205,000. Mr. Clark (*Statistical Journal*, 1929, pt. i.) estimates the seasonal fall in unemployment between January and April for all insured industries *except mining* at 90,500.

quarter of 1924 with the first quarter of 1929, we find that the insured population increased by 684,000, while the number in employment increased by only 509,000; in other words, insured industry had been able to provide for only three-quarters of the additional population dependent upon it. Between the first quarters of 1928 and 1929 there was an actual reduction in numbers employed.

It is difficult to find grounds for optimism in these figures. The *Labour Gazette* of January 1929 analyses the decline in employment in 1928, and finds that it was concentrated in six export industries—coal, shipbuilding, cotton, wool, linen, boot and shoe. This, however, is no mitigation of the evil, but merely confirmation of the diagnosis of the last chapter, especially since the depression in these industries is given as the reason for the decline in employment in the rest of industry.

Our survey of unemployment showed us, however, that the bare figures of recorded unemployment do not reveal the full extent and seriousness of the depression. Account has to be taken of two other factors, the amount of employment that is being given at a loss, and the concentration of unemployment in a limited number of areas dependent upon highly localised industries. The figures illustrating these two factors, given in the last section of Chapter II., are recent enough to discourage belief in spontaneous and unaided recovery. If unemployment does not get better—and apparently it does not—it is likely to get worse, since the strain of working at a loss is cumulative. And the distress in the affected areas and the handicap upon the depressed industries are also cumulative in their effect.

One of the industries in which the unemployment figures concealed the real position was engineering; it reminds us also of another consideration. Judged by the unemployment percentage in it, engineering is less depressed than the average of industry, a remarkable improvement on its state seven and even five years ago. But this improvement is not due to any expansion of employment; the explanation is a decline in the number of persons seeking employment in that industry. Between June 1923 and June 1928 the unemployment *percentage* fell from 17·6 to 8·8; the *number* in employment was practically the same. The apparent improvement in the worst-affected industries has not been due to an expansion in employment.

Contracting and stationary industries are, however, balanced by expanding industries. The exponents of the optimistic view of the future point to these. It is necessary, therefore, briefly to examine the recent tendencies of industrial growth. They are illustrated in the following table:

TABLE V

EXPANDING INDUSTRIES

	Number Insured. Increase, July 1923—July 1927.		Unemployment Percentage.	
	Number.	Per cent.	July 1923.	July 1927.
Distributive trades	327,090	26·1	6·2	4·4
Building and contracting	173,200	20·5	13·1	8·5
Road transport	49,840	19·4	11·2	9·3
Motor manufacture, etc.	41,030	21·4	9·6	7·9
Brick, cement, etc.	35,680	40·5	8·9	4·9
Printing, etc.	28,770	12·6	5·6	4·3
Furniture	20,390	21·7	7·7	4·6
Shipping, etc.	18,730	12·3	18·6	14·3
Electrical engineering	18,340	30·1	7·2	4·8
Artificial silk, etc.	17,770	47·6	6·7	6·6
All expanding	874,740	17·4	..	..

CONTRACTING INDUSTRIES

	Decrease, July 1923—July 1927.		Unemployment Percentage.	
	Number.	Per cent.	July 1923.	July 1927.
General engineering .	66,560	10·0	20·3	9·2
Shipbuilding . . .	53,940	20·0	43·2	22·3
Coal	44,590	3·6	3·0	21·5
Woollen and worsted .	20,240	7·5	9·3	9·5
Iron and steel . . .	16,440	7·8	20·8	18·2
Baking, etc. . . .	12,830	8·0	10·0	5·5
Dress and mantle. . .	11,420	9·7	6·3	4·0
Canal, docks, etc. . .	10,110	5·3	27·1	22·0
Chemicals	8,590	8·3	11·6	6·2
Marine engineering .	8,410	12·8	22·3	13·2
All contracting . .	304,120	7·3	..	..

NOTE.—The total insured population increased between July 1923 and July 1927 by 372,800, or 3·2 per cent. The general unemployment percentage fell between the same two dates from 11·5 to 9·2. The number employed increased by 863,000, or 8½ per cent.

Before any inferences can be attempted from these figures, certain other relevant facts must be brought into account. Insured industry does not cover the whole occupied population, and some additional information is available, which is summarised in the following table. The table is restricted to Great Britain, since the object is to show tendencies, not absolute numbers.

[TABLE

TABLE VI

GREAT BRITAIN

Trends of Employment, 1921–1927

Reference.	1921.	1923.	1926.	1927.
Numbers of insured persons: July . . .	11,080,950	11,231,980	11,773,700	11,875,600
Do. Males . .	7,974,290	8,335,200	8,680,970	8,745,500
Numbers employed by railway companies end of March or beginning of April . . .	735,870	681,778	689,264	683,077
Do. Males . .	708,465	658,883	665,930	658,990
Numbers employed in June on agricultural holdings (excluding occupiers and wives) .	996,081	892,411	920,994	893,724
Do. Males . .	840,968	759,877	786,597	760,522
Number of holdings of 1 acre or more . .	496,136	487,807	478,655	477,600
Total population (estimated for years after 1921)	42,769,000	43,304,000	43,964,000	..
Male population, aged 15-64 (estimated for 1926)	13,309,000	..	13,860,000	..

From the last two tables together it would appear that since 1923 employment has expanded more than population has increased. Before we join in the chorus of congratulations that the contemplation of the figures excites, there are three qualifications to be noted. The first is that between 1921 and 1923 the growth of the insured industries just about compensated for the decrease in employment offered by agriculture and railways, leaving the increase in population to be provided for elsewhere. The second is that, if 1924, instead of 1921 or 1923, be taken as the starting-point of the comparison, we have not been able to absorb in actual employment the whole addition to the insured population. The third is that the increase in employment since

1923 is not the result of a spontaneous and unaided development of the industries that have provided it. Largely it is due to Government subsidies and selective Protection. Of the first seventeen industries, arranged according to rate of increase in the detailed list of expanding industries given in the *Labour Gazette* for November 1927, fourteen have had the advantage, directly or indirectly, of protection or subsidy. Moreover, the largest increases, with one exception, have been provided by industries which work for a demand that is not likely to continue to grow at the rate of recent years. Building and contracting, between 1923 and 1927, drew in 173,200 additional workers, a 20 per cent increase; the building material industries 36,000, a 40 per cent increase. Now that the arrears of housing due to the war have been cleared off, the prospects of further growth, or even the maintenance of the existing numbers, are not good. The motor industry and road transport together drew in 90,000 additional workers, another 20 per cent increase. The domestic market for motors must be approaching satiation, so that the industry's future depends on its ability to secure a larger proportion of the world's export trade, in which Protection and a protective system of taxation will not help it. Road transport, on the other hand, can continue to expand, if the country is prepared to continue expending £55,000,000 a year on roads; but such expansion will be counteracted in part at least by a further decline in railway employment. And so with the other industries—gramophones, artificial silk and the rest, which cut such an imposing figure in Stock Exchange speculation, and such a trivial figure in industrial employment; they offer no alternative to which the country can turn, if the decline in

the older staple industries cannot be arrested. The 48 per cent increase in the numbers engaged in silk and artificial silk between 1923 and 1927 was insufficient to compensate for the $7\frac{1}{2}$ per cent decline in woollen and worsted, while the 38 per cent increase in the "key" industries of scientific instruments and photographic apparatus would not balance the closing of a couple of good-sized mines. The one employment that expanded without the aid of Protection or subsidies was the largest, the distributive trades. This growth is a perfectly natural development, the corollary of increasing economy in manufacturing production; but, again, it offers small prospect of replacing the employment lost in the staple industries. On the contrary, the expanding costs of distribution, by keeping up retail prices when wholesale prices have been brought down, check the demand for the products of industry and so delay recovery.

The expanding industries, therefore, offer no adequate substitute for the loss of older trades. Since 1927, when the building subsidies were cut down, the expansion of the building and house equipment industries has been checked. The decline in the number of work-people employed (*i.e.* insured less unemployed) in coal-mining and engineering between 1924 and 1929 was about equivalent to the aggregate increase, in the same period, in employment afforded by all the expanding industries other than building and contracting and retail distribution. And recently unemployment has shown a tendency to increase in these hitherto favoured industries.

To sum up: the persistence of unemployment on an abnormal scale, its increase in the last year, the insecurity of much employment that at present is

being given at a loss, the concentration in particular localities, taken with the inability of the recently expanding industries to take up the surplus labour of the contracting industries, forbid an easy optimism that would rely on the unaided expansion of industry to solve the problem of unemployment. It follows also that the measures hitherto adopted have been inadequate to their object. To these we will turn next.

II. *Recent Expedients*

a. Selective Protection

The attempt has been made to stimulate industrial expansion, or check contraction, by safeguarding, or —to use the more familiar equivalent of Latin origin— *protecting* domestic manufactures against foreign imports. The effect of the protection hitherto given is indecisive, because it has been applied in two important cases to developing industries, which might have expanded in any case. It is to be expected, however, that protection will benefit the protected industries; it is with its indirect and aggregate effects that we are concerned.

It is a remedy that is applicable only to an insignificant fraction of the unemployment which it is desired to remedy. In a careful analysis of the incidence of unemployment at the end of 1928 and its relation to import and export trades, *The Economist*[1] showed that two-thirds of all the unemployment at the time was in industries that were "unprotectable", either because, like mining and shipbuilding, they had no imports to compete with, or, like building and retail distribution,

[1] Issue of February 2, 1929.

competitive imports were impossible. Of the remaining third much the greater part was in industries that were predominently export industries. If *The Economist's* view be taken, that protection cannot help an export industry, since it is impossible for it to protect a foreign market, only one-fortieth part of unemployment could possibly be benefited by protection.

The advocates of this policy, however, argue that export industries can be assisted by protection, and their argument requires examination. It is, that a protective duty, by securing to it the home market, will enable the home industry to work full, and so to secure the economies of full-time production. Assured of these, it will be in a position to cut prices in the export field. The argument confuses scale with volume of production. The increase in *volume* of production, that protection might stimulate, could take the shape either of a multiplication of firms in the protected industry, without any increase of scale, or of an increase of *scale* without any increase in the number of firms; only on the latter hypothesis would there be much reduction in costs. Thus protection by itself is insufficient; a concentration of production is needed in addition. Indeed the possible economies are due to concentration and full-time working; and the same results as are expected from protection could be attained if the Government gave any other inducement to concentration and full-time working, *e.g.* by offering to provide credits for large-scale contracts.

There is another limit to the utility of selective protection. Except when it provides a stimulus to an industry that is capable of expansion for other reasons, and only needs an initial impulse and nursing, its effect is merely to divert production from unprotected

to protected channels. A fair example of the refusal to face the secondary effects of protection was the speech of the Minister of Labour in the debate on Unemployment in the House of Commons on March 25th. He attributed the present abnormal unemployment to two chief causes; first, the falling off in emigration since the war, which had meant an extra 300,000 to 400,000 on the labour market here;[1] and second, the falling off in the volume of our foreign trade, which had meant the unemployment of from 700,000 to 800,000 in this country; safeguarding, by keeping work for them which could just as well be done in this country, would meet the needs of the unemployed workers in the first category; de-rating would provide for some of the 700,000 or 800,000 in the second. Now the net output (gross value less materials—net output is taken so that imports and exports represented by foreign raw materials can be left out of account) per head of the industrial population, as shown by the 1924 Census of Production, was £220. Taking the mean figure in each case, the effect of the measures indicated, assuming they were adequate to their end, upon the foreign trade balance of the country, would be to decrease imports by £77,000,000 (£220 × 350,000) or rather more than a quarter of the total of "manufactured and mainly manufactured" imports in 1928, and increase exports by £165,000,000, or 23 per cent of the total exports of United Kingdom produce in 1928.

Is it likely that this country, with its high internal level of costs compared with world prices, would be able to induce the rest of the world to take £165,000,000 worth more goods at the time when we were reducing

[1] This seems to overlook the loss of 700,000 men of working age, killed in the war.

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our takings of their goods, and therefore their sterling resources, by £77,000,000? The Reparations Transfer is a simpler proposition. Some readjustment within the categories of imports might be possible, other countries sending us more products that did not compete with ours; but our demand for food-stuffs and other non-competitive products is relatively inelastic, and other countries' activities cannot easily be changed into new channels. The probable effect, therefore, of any success on our part in excluding competing manufactures, would be simply to divert them from our home to our export markets, which we should lose, if we could not cut prices below the level that would have sufficed, without protection, to keep them out of the home market.

A change in this direction in the balance of our trade relations with other countries would involve also a great increase in our export of capital; refusing to take goods for goods, we should have to supply our additional exports on credit. *If* we could re-employ 750,000 men, we could doubtless afford to lend an additional £100,000,000 or so abroad. The export of capital has not, however, the same certainty of effect, in a corresponding export of goods, as it had before the war. Then foreign borrowers were mainly merchants and industrialists, who could not afford to keep idle the sterling balances they acquired by our loans; to-day, Governments are the biggest borrowers in the international loan market, and the sterling balances, which our export of capital puts at the disposal of other countries, may very well come into the hands of some foreign Government or Central Bank, which finds it convenient or necessary to keep large balances in London against obligations due to America or other countries;

and such balances must be kept in a liquid form, not converted into exportable goods, even at some loss.

The probable effect of selective protection, then, is to divert, not to add to, the country's economic activities. We make more things at home; foreigners therefore can buy less from us; and those export industries, which are specialised to foreign markets or already in complete possession of the home market, like cotton and coal, find their difficulties aggravated. The expansion of the protected industries is balanced by the contraction in the predominantly export industries, and there is no reason to anticipate that the exports of the protected industries will supply the place of those of the contracting industries. Doubtless the exports of the motor industry, for example, will grow, but they have some way to go before their proportion of the world's export trade, at present about 6½ per cent, approaches that of cotton or shipbuilding, both of which, even in their present depressed state, do more than half the world's total export trade in their respective fields.

b. Transfer

The transfer of workers from declining to growing industries is a normal process. It had done more to relieve unemployment, by reducing the numbers of insured workers in the depressed engineering, shipbuilding, and metal group of munitions trades by 400,000, without any special Government recognition or assistance, than any other agency had done, before it was recommended as an instrument of deliberate policy by the Industrial Transfer Board. Much of this redistribution, it is true, had taken the form of checking the entry of juvenile workers to fill the places of

workers who had died or retired; but much also was the result of the spontaneous movement of adult workers from one trade or district to another. Anything that Government can do, therefore, to encourage and facilitate such redistribution will be a contribution, as productive as it is direct, to the relief of unemployment.

Such measures will fall into three heads; the placing of labour in districts with expanding industries and the grant of financial assistance towards removal expenses; training and re-training to enable displaced workers to take advantage of openings in other industries; and negative measures directed to removing obstacles to transfer.

In the period from August 1928, when the Prime Minister appealed to employers to assist transfer by taking on workers from the depressed areas, to the end of April 1929, 20,700 persons were transferred by the Ministry of Labour's machinery; 2315 of these had received training in one of the training centres for men, 1885 were boys, many of whom had received some re-education in the 102 juvenile unemployment centres, 941 were women and girls trained in the 38 centres of housecraft training. These numbers represent a great *absolute* benefit conferred on unemployed workers, but a very small *relative* impression upon the problem of unemployment.

The possibilities of classifying the unemployed and applying educational and remedial treatment appropriate to the needs of the different classes, have been examined by Mr. Davison, to whose work reference may be made.[1] Such retraining is necessary if transfer is to extend. More especially is it necessary with one group of unemployed. In general personal defect will

[1] *The Unemployed*, by R. C. Davison. Longmans, 1929.

not explain post-war unemployment. The unemployed are not an identical collection of individuals from month to month, but a pool through which a stream is flowing; half of the total registrations of unemployed in each month are new. The Ministry of Labour has conducted a series of sample inquiries into the personal and industrial character of the unemployed; while the classification is necessarily rough, it represents the judgment of experienced Employment Exchange officials, who are in continuous contact with labour of all kinds. The most recent inquiry, which confirms the results of the previous inquiries, shows only 3·6 per cent of unemployed males and 1·4 per cent of unemployed females in the category "verging on unemployability"; while 62·7 per cent of the males and 77·2 per cent of the females would normally be in steady employment.

But one age group of males has a weight in the unemployed population out of proportion to the weight it has in the occupied population. It is the group aged 25-29, and to a less extent the group 30-34; together these groups include 28 per cent of the unemployed males as against only 23·6 per cent of the occupied male population. The men in these groups are the lads who came into industry during the war, or had their industrial training interrupted by the war. They were sucked into the munitions industries, and set to work which fitted them for nothing when peace returned.

Measures directed to removing obstacles to redistribution of labour would include some reconsideration of the Unemployment Insurance Scheme. It is not that unemployment relief leads to the refusal of available work; the Employment Exchanges provide an adequate check on that abuse, were there any general

inclination towards it. Nor does the relief, as it is administered, impose any insuperable check upon mobility between district and district or trade and trade. The Courts of Referees and the Umpire, who decide on doubtful claims to benefit and administer the provisions in the Acts that the applicant shall be "genuinely seeking work", and shall not refuse an offer of "suitable employment", while they treat each case on its merits, have in general put an interpretation upon these conditions that requires the unemployed workman sooner or later to accept work outside his own district or trade, if it is available. It is the special method of dealing with temporary unemployment that may be delaying transfer. The system of organised short time makes it possible to dovetail periods of wage-earning with periods of unemployment relief. Right to benefit under the Unemployment Insurance Scheme does not begin the moment a worker falls out of employment, but only when a waiting period of a week has elapsed; any three days of unemployment, however, within six consecutive days, or two unemployment periods of at least three days each separated by a spell of not more than ten weeks' work, are treated as continuous unemployment, and a second "waiting period" is not required. Employers have adapted their engagement of labour to these conditions, and thus spread the available employment over a larger number of workers than the industry could employ full-time, at the same time throwing on the unemployment insurance fund the burden of maintaining the surplus labour when it is not in employment. Instituted as a device for tiding over a temporary depression, this system has been prolonged as year succeeded year of unemployment, and has had the effect of substituting

intermittent and irregular employment for regular work in industries in which such conditions were formerly rare.

The figures that have been given, however, 20,000 in eight months, are sufficient to indicate the limits of the scheme. Transfer may in the course of years bring about a more even distribution of the burden of unemployment; it can increase the volume of employment only when it satisfies a hitherto unsatisfied demand for labour, and of such unsatisfied demands the Industrial Transfer Board produced no evidence.

Had it greater possibilities, transfer by itself is open to some economic objections. It may take two forms, transfer within the country and assisted emigration. Now transfer within the country, as a remedy for the distress of the areas in which depression is concentrated, may involve costs that the employment elsewhere of the transferred workers will not counterbalance. It would relieve those workers from Durham and Glamorgan, Oldham and Jarrow, whom it placed in employment elsewhere; but it would do nothing to relieve the secondary losses due to the depression in the industries on which such localities were dependent. An industrial community, even a mining village, embodies a considerable social capital (over and above the capital in the dominant industry) in shops and houses, neighbourhood trades, schools, and the whole complex of local economic services. Assume that the capital in the dominant industry must be written off as a loss; is it necessary to destroy the value of all the rest, by taking away the labour that alone can maintain its value? Should not every possibility of finding a substitute for the declining industry be explored before adopting such a policy of despair?

The location of new industries is largely a matter of

accident; how otherwise account for the establishment of the largest British motor works in the playing-fields of a disused military academy on the outskirts of Oxford? It is influenced by a desire to avoid high rates and trade union control of wages and conditions. If the benefits of de-rating had been concentrated upon the depressed areas, they might have sufficed to attract new industries to them. The decline of localised industries has not in the past prevented the rise in the same localities of new industries to take their place. The decline of the Yorkshire linen industry did not involve the depopulation of Leeds; nor did the shift of the iron and steel industry from the Midland Black Country to the coast leave that area without employment. In circumstances like the present, the location of new and developing industries might surely be made an object of conscious consideration and deliberate public policy; with Lancashire and South Wales already industrialised, it would have been cheaper to assist and encourage the utilisation of their resources in new directions, by differential rating and taxation, by making location in a depressed area a condition of any form of protection, by State-guaranteed loans to new enterprises in such areas, by any other form of State assistance that may be adopted—before low wages and low rates were allowed to draw capital and enterprise to new industrial districts, and involve the country in the costs of converting agricultural areas into new towns.

Transfer abroad, by assisted emigration, raises similar considerations.[1] It involves the sacrifice of an

[1] Unassisted emigration is not a remedy for unemployment, since it rises with prosperity, as the Colwyn Committee point out, and sinks with depression.

asset, a man whose upbringing has cost the State and the community some hundreds of pounds before he began to contribute to the economic wealth of the country. It is limited by the capacity of the Dominions to absorb new labour, which in turn depends on the rate of capital application and development in those countries. The Dominions draw capital for this purpose largely from the English capital market, since the stock of Colonial Governments enjoys the status of trustee securities in this country, which loans used for precisely similar economic purposes by British municipalities and public utilities do not enjoy. The capital so acquired releases local capital for the development, behind tariff walls, of local manufactures, that compete with British exports. Is not this an unnecessarily roundabout way of providing work for British workers? It is not a wild speculation that an equivalent sum, expended in establishing new industries or re-equipping existing industries in this country, would enable them to provide employment for more than the number of subsidised emigrants. Meanwhile the Scottish Nationalist complains that the Imperial Government, which will spend thousands in assisting Scotchmen to leave Scotland, will do nothing to provide for them at home, and that although it costs £1500 to settle a man in Australia and only £360 to settle him on a farm in Scotland, there are 8226 outstanding claims for new or enlarged holdings awaiting the attention of the Scottish Board of Agriculture.[1]

c. De-rating

De-rating approaches the problem more closely. The high level of costs in relation to world prices is the

[1] *The Re-Discovery of Scotland*, G. M. Thomson. Kegan Paul, 1929.

chief explanation of depression, and de-rating attacks costs. It is no criticism to point to the small proportion rates *as a whole* bear to industrial costs *as a whole*, The effect must be judged in relation to products, in which rates form an important proportion of costs, and evidence was placed before the Balfour Committee showing that on finished steel the increase in costs attributable to local rates varied from 4s. 5d. to 7s. 2½d. per ton. Nor is it a valid objection that the relief is given to prosperous as well as to unprosperous industries and firms. If the prosperity is based on conditions that may be expected to last, there is every reason for giving the expanding industries and firms the same assistance as the depressed ones, since unemployment is likely to be permanently relieved by their expansion. In so far as their prosperity, however, was due to the advantage of location in a lightly rated area, it is a valid objection; and we have seen that the unequal burden of local rates is one factor in causing inequality of fortune among industries. It is unfortunate, therefore, that the relief was not more directly related to the needs of different areas, as measured by the extent of able-bodied pauperism due to unemployment, and concentrated on those districts in which depression could be directly attributed to the temporary effects of the war. The £26 millions relief would in that case have been enough to effect a real change in the condition of the depressed areas, and might even have been enough to attract new industries to them. As it is, the relief is spread too thin, and will be an effective restorative in very few cases. Since it is applied in the same proportion to all areas, the relative attractiveness of different areas will be unchanged; if a firm preferred Essex to Durham before the change,

because rates were lower, it will still prefer Essex, because rates will still be lower in the same proportion.

High Poor Rates and low assessable values are the chief explanation of high local rates; and both of them go with a high unemployment rate. Dr. Mess has given illustrations of the relative rise since 1914 of local expenditure per head of population on different services.[1] In Newcastle total rate expenditure other than Poor Law expenditure rose from 28s. to 51s. 6d. per head, Poor Law expenditure from 6s. 3d. to 35s. 7d.; in South Shields other rate expenditure from 20s. 10d. to 37s. 5d., Poor Law expenditure from 5s. 3d. to 23s. 5d.; in all county boroughs in England and Wales other rate expenditure from 29s. 7d. to 55s. 1d., Poor Law expenditure from 5s. 6d. to 15s. 10d. In other words, other local expenditure from rates has risen little more than proportionately to the rise in prices, if Poor Law expenditure be left out of account; Poor Law expenditure shows a much greater and a much more unequal rise. The de-rating scheme, whatever its merits in relation to other aspects of local and central finance, missed an opportunity of cancelling one important handicap that the depression has imposed upon the export industries.

The relief was wastefully applied for another reason. It was given to firms and even industries which will not, as a result of the relief, necessarily increase or even maintain employment. Where a firm or an industry enjoys any element of monopoly, it endeavours to regulate its prices or charges and output in such a way that it secures a maximum of receipts over expenses. To increase employment, it is necessary to lower prices and stimulate demand. If the monopolist knew his business

[1] *Industrial Tyneside*, ch. xi. Benn, 1928.

and had fixed output at the point that gave him the maximum return, it might not pay him to lower his prices; he would then pocket the whole of the reduction in rates, without using any of it to lower prices and increase output. It would pay him to reduce prices only when the economies of a larger output would compensate, not only for the lower price, but also for the loss of monopoly profits on the smaller output. It is unlikely, for example, that the railways of their own initiative would have reduced their charges by the amount of rate relief they receive, or that brewers will find it pay them to do so, or that the textile-finishing combines will hand over the relief to their customers in preference to their shareholders. When demand is inelastic, that is to say, at a point at which a large reduction in price is needed to stimulate a small increase in consumption, it will certainly pay the monopolist better to restrict output to the previous amount, and keep the relief for himself; even competitive industries, faced with such a market situation, would be able to increase employment very little by using the whole relief to cut prices.

III. *The Expansion of Public Enterprise*

The expedients discussed in the last section did not by themselves constitute a policy. They were merely incidental and supplementary to a policy of relying on private enterprise. Left to itself, it is hoped, private enterprise will reorganise industry, so far as that is necessary to reduce costs, and find a way out of the present difficulties; protection will give it a stimulus, de-rating will ease its task, and transfer will provide for the residuum that no revival of industry can be expected to float. Opinion on these expedients will, there-

fore, depend, not on their value in isolation, but on the judgment formed of the capacity of private enterprise, unaided otherwise, to restore industrial activity. The alternative opinion, we saw, was that unemployment was too severe and too prolonged to be left to the unaided efforts of private industry. It is necessary to examine, briefly, the policy associated with this view also, for the light it throws on the nature of the unemployment problem.

The form in which the policy has attracted most attention is in the proposals put forward under the auspices of Mr. Lloyd George.[1] Briefly their object is to increase employment out of loans upon works of public utility. The policy is related specifically to the present emergency, and the actual proposals are confined to works normally undertaken or assisted by public authorities, in order that they may be put in hand at once by public initiative. The basis in principle of the policy is indicated in the following quotation:[2]

> We believe we can throw off the national shoulders this Old Man of the Sea of unemployment, if we have the will, and if we follow the large scale and definite policy which we now propose. We have the men, the money and the management; put together, these mean goods and services for the benefit of the whole nation. Let us put them together. . . . At the moment, individual enterprise alone cannot restore the situation within a time for which we can wait. The State must therefore lend its aid and, by a deliberate policy of national development, help to set going at full speed the great machine of industry. . . . At the very least, by such a policy, we should save multitudes of our fellows from demoralisation or despair; we should help to bridge

[1] The proposals were associated with an undertaking to reduce unemployment to normal proportions in two years, which it is unnecessary to discuss.

[2] *We can Conquer Unemployment*, Cassell. Cf. *Can Lloyd George Do It?* by J. M. Keynes and H. D. Henderson, *The Nation*.

over that difficult period in which our industries are recovering their competitive position in the world's markets; we should stop a large part of the waste of the nation's finest resources, its labour power; we should improve our national estate and increase our national efficiency. At the best, we should give just that stimulus which is wanted in the present condition of economic inertia to set industry moving vigorously again on the normal line of progress. Perhaps it is a venture of faith, but the present is a situation which demands faith as the alternative to despair.

It should be noted, in the first place, that public expenditure on works of public utility has been used throughout the depression to mitigate its effects. On an average 100,000 men, it was claimed by the Governments of the day, were so employed from 1923 to 1926. If then, as Mr. Churchill stated in his Budget speech in 1929,

> it is the orthodox Treasury dogma, steadfastly held, that whatever might be the political and social advantages, very little additional employment can, in fact, as a general rule, be created by State borrowing and State expenditure,

we can only conclude that the Treasury has hitherto been unable to commend its dogma to its principals. This figure of 100,000 is exclusive of the employment afforded by the expansion of building and the related industries under the stimulus of housing subsidies. Ministers who have claimed the credit in the past of providing work by public expenditure are estopped from criticising the principle, as distinct from the details and extent of a policy of expanding such provision in the future.

In the second place, it should be noted that the policy takes credit for anticipated savings in unemployment insurance and poor relief. The value of the work

done, therefore, has only to equal the difference between the cost of relieving the workmen employed and paying them wages, in order to provide an economic justification for the employment. Actually it is claimed that the works proposed would have a value to the country that by itself would justify them, without taking account of any reduction in unemployment relief. It is assumed that the works will in fact increase, not merely divert, employment; the question of theory we have now to examine.

In turning to this question of principle, it is useful to distinguish between the immediate and the ultimate effects upon unemployment. The policy is put forward primarily as an emergency measure to provide employment until industry in general recovers; but it is also claimed for it that, by maintaining the quality of the working population and reducing the economic waste involved in traffic congestion, inadequate electricity supply, bad housing conditions, and other remediable evils, it will reduce costs, and so accelerate the recovery, the delay in which makes it necessary. In another and even more important way it is claimed it would assist recovery; for it would bring into play what Mr. Keynes and Mr. Henderson call "the cumulative force of trade activity":

> The fact that many workpeople who are now unemployed would be receiving wages instead of unemployment pay would mean an increase in effective purchasing power which would give a general stimulus to trade. Moreover, the greater trade activity would make for further trade activity; for the forces of prosperity, like those of trade depression, work with a cumulative effect. When trade is slack there is a tendency to postpone placing orders, a reluctance to lay in stocks, a general hesitation to go forward or take risks. When, on the other hand, the wheels

of trade begin to move briskly, the opposite set of forces comes into play, a mood favourable to enterprise and capital extensions spreads through the business community, and the expansion of trade gains accordingly a gathering momentum.

The opposite view has been indicated in the quotation from Mr. Churchill's Budget speech given above. It is held that the additional expenditure must either be financed by inflation, which the Liberal pamphlet (p. 62) rules out, or it will merely divert employment from enterprises at present initiated by private enterprise. In the absence of inflation, new schemes can be financed only out of current accumulations of capital, and, if these are taken for public enterprise, they will not be available for private enterprise. Further, since already 63 per cent, on the average of the last four years, of the new capital issues on the London market are on home account, as against 19·3 per cent in the four years before the war, the diversion must be from capital exported; since the reduction in capital exports is a principal cause of the depression in the export industries, whose products used to be bought with our overseas loans, the policy would make unemployment worse. Apart from its reactions on employment, the policy, by increasing the competition for capital, especially in the overcrowded Government security market, would force up the rate of interest, increase the burden of debt, and prevent conversions that would lighten it. To the argument of the Liberal pamphlet, that the rise in Bank deposits and the rise in the proportion of time deposits to demand deposits indicates a superfluity of savings awaiting investment, the reply is made that these represent the loose cash of temporarily inactive business firms and balances kept in London by foreign banks and institutions, both of which must

be kept liquid and are not available for long-term investment.[1]

Without attempting to follow into detail the controversy between these two views, it may be pointed out that the Treasury argument proves too much. On that theory of the relation of industrial activity to capital accumulations, there could be no increase in industrial activity without a prior or concurrent increase in savings. It makes no necessary difference to the volume of employment provided, whether capital is applied by private industry or public enterprise; if an expansion of public enterprise would merely divert employment, an expansion of private enterprise would have the same effect, and there can be no improvement in trade, until more capital is accumulated. The argument seems to assume a doctrine of a fixed *Capital Fund*, a variant of the Wages Fund theory and open to the same criticism. Industry has expanded after trade depression in the past, without any prior increase in capital resources, because the expansion itself provides the resources out of which expansion is possible. The problem is to find the causes that stimulate expansion, and the placing of a large number of Government contracts might be one of them.

On the Treasury theory, the £73 millions spent on roads, £48 millions on telephone extensions, and £133 millions on housing in the last four years must have been diverted from private enterprise, which would have used them to provide employment. The loans to Kenya and other colonies made in the past, and the loans proposed for further colonial development, fall under the same criticism. We are in danger of reducing the controversy to a difference between those who

[1] Cf. Memorandum prepared by the Treasury in Cmd. 3331.

believe that public loans can be used to promote employment only if they are expended in the colonies, and those who believe that they will equally well promote employment if they are expended in England. The Treasury seems to assume that there is a constant relation between savings and investment; Mr. Keynes and Mr. Henderson point out that this is not the case. Sometimes investment runs ahead of savings, when there is inflation of credit and a boom; sometimes investment lags behind savings, and idle deposits accumulate in the banks and there is a depression. To provide, by Government borrowing for public works, an outlet for or stimulus to the use of these savings, is not inflation; inflation begins only when labour is fully employed and the demand for capital is pushed beyond the point at which it can be satisfied out of savings.[1]

The controversy turns ultimately on the relation of credit to industrial expansion. If we leave money and credit out of account, there is obviously no theoretical impossibility in employing men, who at present are being kept doing nothing, on plant which is also idle, at any useful work within their capacity and for which materials are available. It is the complications of a money economy that make it difficult. This aspect of the problem has been examined by Mr. Hawtrey in an essay that was written, fortunately, before it became

[1] The increase in bank clearings in a period of falling commodity prices might seem to prove that deposits are being turned over more, not less, rapidly, and to disprove the contention that idle deposits have accumulated. But the figures of clearings are influenced very much by stock exchange speculation, and, if commodity prices have fallen, stock prices have risen. The objection that a large part of the deposits would not be available for public loans, being cash resources of firms that have no present use for them, is not decisive; if the firms have no use for them and have placed them on time deposit, they could invest them in the Government loans, which would be a liquid enough form in which to hold them.

a subject of political controversy.[1] Employment depends on demand, which depends on consumers' outlay, which in turn is limited by the means of payment available. If the expansion of Government enterprise is accompanied by no expansion of credit, it cannot increase employment, because there is no addition to the means of payment, and the Government merely diverts consumers' outlay from the commodities and investments they would otherwise have bought to its own purposes.[2] There is, however, an exception to this: "in a period of depression the rapidity of circulation is low, because people cannot find profitable outlets for their surplus funds and they accumulate idle balances. If the Government comes forward with an attractive gilt-edged loan, it may raise money, not merely by taking the place of other possible capital issues, but by securing money that would otherwise have remained idle in balances" (*op. cit.* p. 110).

The hypothesis that no expansion of credit would take place is, however, unlikely, if not unreal. In fact the additional means of payment, which will make an addition, and not a mere diversion, of employment possible, can be found by increasing bank credits. Since a Government loan is an excellent security for bank credits, probably such an expansion will take place. This does not prove, however, that the policy is sound. It is not the Government expenditure, but the expansion of credit which it involves, that gives the additional employment; and the same result might be attained by a creation of credit unaccompanied by

[1] *Trade and Credit*, vi., Longmans, 1928.

[2] There may be differences in the amount of employment afforded by different kinds of expenditure, but there is no reason to suppose that the amount would be greater if the Government did the spending, since we are not concerned with relief works selected for the high proportion of labour they involve.

public works. "To resort for the purpose to the construction of expensive public works is to burn down the house for the sake of the roast pig." This case also, however, is subject to an exception. If the ordinary methods of credit expansion have been applied—the effect of a low bank rate reinforced by purchases of securities on the part of the bank in the open market—and proved insufficient restoratives, there would be a case for having recourse to Government borrowing. But Mr. Hawtrey does not think that such recourse would ever be necessary.

It is arguable that Mr. Hawtrey's two exceptions both cover the present condition of British industry. Idle balances have accumulated and need some stimulus to make them active. Mr. Hawtrey insists that it is not the public expenditure but the public *borrowing* that influences employment; put it rather that, in the absence of enterprise on the part of private borrowers, public enterprise is necessary. Admitting the importance of foreign balances, it is nevertheless significant that, at the beginning of the present year, bank deposits had practically reached again the peak they reached in the post-war boom, while, owing to the fall in prices, they have two-thirds greater purchasing power.[1] While German industry is hampered by a lack of liquid resources, we have a superfluity, which is used to finance speculative issues and to sustain an inflated level of industrial security prices. And, as we saw in our analysis of pre-war cycles, an accumulation of inactive deposits was a characteristic feature of depressions, and movement of them a normal condition of recovery.

	Deposits £ Million.	Wholesale Price Index.
[1] January 1921 . . .	1850	246
,, 1929 . . .	1843	140

The other exception is equally applicable, though for reasons that Mr. Hawtrey does not consider. The ordinary inducements to credit expansion cannot be used. It is impossible for the Bank to lower bank rate or supply the market with money by purchase of securities, because the money so provided would simply be drained away to New York. The use of liquid funds at high rates of interest to finance stock exchange speculation in New York has introduced a novel complication into monetary policy; and, although the conditions of British industry are such as call for Mr. Hawtrey's prescription of lowered bank rate, it is impossible to apply it without causing such a flow of funds to New York as would endanger the Gold Standard and compel a drastic raising of the rate again. Public expenditure in this case may offer the safest means of expanding industrial activity without endangering monetary stability; any additional credit created would be used to finance production at home instead of stock exchange speculation in New York.

The fundamental objection in principle, then, that public enterprise would merely divert without increasing employment, does not appear to be well founded. The case for the policy rests on less obscure and more obvious considerations: Is there work of public utility waiting to be done? are there savings available for application to it? and would the application tend to assist a revival of trade that would provide employment when employment out of public funds was eventually curtailed?

The first of these questions turns on technical considerations, which the present writer is incompetent to discuss. *A priori* it seems unlikely that Great Britain alone of all the territories in the British Empire

would not repay some further expenditure of public funds on economic development; it is almost as unlikely that development work could reduce unemployment by 700,000 or 800,000 inside two years. The accumulation of bank deposits suggests that openings for investment are lagging behind savings. If a series of Government development loans did divert some savings from the type of speculative issue that has found most favour with investors in recent years, it would be a benefit to the investors, who would be less likely to lose their investment, and to the country, which would have something, even if only roads and houses, to show for the expenditure of the savings. For the purpose of the present inquiry, however, the most interesting question is the long-term effect of large public expenditure on capital works upon trade revival.

We have seen that the proposal is put forward only as an emergency measure, which would be justified by the demoralisation it prevented, even if it did not improve the prospects of trade revival; but it is claimed also that the "cumulative effects of trade activity" might swing industry round on to the upward grade again. Against the obvious benefits must be set certain possible adverse effects—the locking up in temporary public works of labour that might have been absorbed in expanding permanent employment, the check to a necessary redistribution of labour to meet the changes in the post-war world, the increase in the costs of industry which any miscalculation and waste would involve in additional taxation and raised wage-rates. The White Paper, in which the Government of the day replied to Mr. Lloyd George's pamphlet, if it proves nothing else, proves that the departments concerned

are fully aware of these dangers; but they might not be able to avoid them in giving effect in two years to a programme they would normally have spread over ten.

The programme might conceivably reduce the costs of industry and so encourage revival. But most of the objects of expenditure, though socially desirable, would not remove any serious elements in the costs of industry. Capital might be applied in ways that would effectively reduce costs; but not under public authorities. Most of the older industries would benefit by re-equipment on a large scale, which they cannot afford out of any resources they can command on their own credit; they are handicapped in competition with continental producers whose industries have been re-equipped; but such capital expenditure is not the proposal.[1]

The programme might also reduce costs by making commercially possible a larger volume, and therefore a larger scale, of production. It would have, then, the same justification as is claimed for Protection, or that Mr. Hawtrey claims for a direct creation of credit. Public works with this object are very suggestive of burning down houses to roast pig; but the dearth of private enterprise may make public enterprise necessary.

With these qualifications, however, it is not clear how the programme would have any effect outside the direct provision of employment. If the undertaking of public works increases employment, their suspension should reduce employment in the same degree. Private enterprise does not flag without a reason, nor does industry recover without some more tangible reason than "the cumulation of activity". To rely on the

[1] Cf. *infra* ch. vi.

latter is to take a view of trade depression and recovery as self-generating and psychological, which neither our analysis of pre-war cycles nor our study of recent conditions supports. Trade depression before the war was cured by bringing down costs to a level at which production could expand without loss. Recovery has been delayed in recent years because prices have been brought down while all the chief costs of industry have remained high. We are brought back to the relation of costs and prices. Debarred by the Gold Standard from doing anything to raise prices again, we have no alternative except to bring down costs. A programme of public expenditure must be regarded, therefore, as an emergency programme, and must not divert attention from the long-term needs of industry. And in carrying it out, in the interest of these needs, it must be limited to works that justify the expenditure on them, costs must be kept down, and any attempt to exploit Government demand to raise wages—as the munitions and housing programme were exploited—must be resisted.

IV. *An Obstacle to Expansion*

The difficulties of the greater export industries have claimed the greater part of our attention, because unemployment is concentrated in these and in the districts that depend upon them, and because the danger of further contraction is greatest there. Nor is this attention excessive, if we look to the future instead of to the past. The contribution to the relief of unemployment which a very slight recovery in the cotton or engineering industry might make is much more important than a large percentage increase in the

production of artificial silk, gramophones, automatic machines, or cigarettes. Although complete recovery is improbable, a partial recovery may reasonably be expected from two sources—the growth in world demand and an increase, if costs can be brought down, in the British share of world production for export. In spite of the war and post-war dislocation, the recent Census of Production showed that a fifth of the coal, a third of the iron and steel, a quarter of the general engineering, half the shipbuilding, four-fifths of the cotton, and more than half of the woollen and worsted were for export. Before the war there was a steady growth in the demand for these products, in spite of the simultaneous growth of competing manufactures in other countries; in other words, world demand grew as rapidly as world productive capacity. The war and the post-war confusion checked the growth of world demand, while stimulating the growth of productive capacity; but the International Economic Conference reported that the increase in wealth had been resumed. The world is growing in population and resources, and the older export industries, on a long view, just because they work for elementary needs and a world market, are not worse situated than industries, like building, which have expanded in response to a temporary and satiable demand in the restricted home market.

On a short view, unfortunately, they are worse situated. Their plight is paralleled by the similar plight of the same industries in all or most other countries. There is excessive productive capacity, to which the world has not yet grown up; so that, with the utmost assistance from existing industries, new industries will be needed to absorb the increase in the

population and compensate for the contraction in established industries. Now, before the war, although we had no measure of industrial expansion, it is quite clear that expansion was adequate and continuous. Population was increasing at a greater rate than now, yet there was no cumulative problem of unemployment, and the standard of life of the population was steadily rising. And this expansion was so automatic and easy that we were hardly conscious that it was taking place. To-day we need expansion at a similar rate to relieve the accumulated mass of war-induced unemployment, and are unable even to keep pace with the diminished growth of population. The life and resilience, which kept the problem of employment within limits before the war, have been weakened.

Now the chief source and means of expansion, then as now, was the profits of existing businesses, placed to reserve or otherwise reinvested. The industrial North seldom came to the London capital market for new capital; on the contrary, London was the channel through which the savings of the professional and *rentier* classes in this country were directed abroad. And not only the capital; the enterprise that applied new capital to British industry was supplied by the men who were engaged in the conduct of existing businesses. British industrialists owed little, if anything, to Government assistance or the initiative of outside financiers. The growth of industry was due entirely to the industrialists actually engaged in industry. A change that the war brought about is at once obvious. This class was subjected to an amount of direct taxation to meet the costs of war and of post-war extension of social services, not indeed heavier than that imposed on other classes in the country, but far heavier

than that which the corresponding class in any other country had to bear. While price inflation was transferring to German, French, and Belgian industrialists a large part of the wealth of other social classes, not only was deflation exercising an opposite influence on the British industrialist, but taxation at the rate of 5s. in the £, with a varying amount of Super Tax in addition and Death Duties at intervals, was depleting such profits as he could still secure. And this taxation did not discriminate between the profits he spent and the profits he used to expand his business.

The placing of profits back into business is much the most economical application of new capital. It ensures that capital will be applied only where management has shown its capacity to use capital effectively, and only where the possibility of using new capital to advantage has been demonstrated. Savings applied to establishing new businesses through new issues are frequently lost, and give no additional employment, either because the project to be financed proves unsound or the management unequal to its task; profits applied by the management that has made them to the expansion of the project or type of project by which it has made them gives the best possible assurance against such loss. Anything, therefore, that encourages the application of profits to further expansion, instead of their distribution in dividends, anything that makes possible the application of larger amounts in this way, applies a stimulus to industry automatically at the points where the stimulus must have most effect. Both the industries that are best able to expand, and the firms in each industry that are best able to expand, will be encouraged and enabled to expand.

The amount of stimulus that can be and is applied

to industry in this way depends obviously on the profitableness of industry, and is largely independent of the action of the Government. Expansion was adequate to absorb the increase in the population before the war, because profits were adequate. In America since the war expansion has been so rapid that wages have risen while prices fell, because profits have been so large, and immense sums could be reinvested annually in industry. Even in this country a large proportion of profits have been so reinvested; without them employment could not have been even maintained without lowering the standard of life; but the amount has been relatively less than before the war in the depressed industries just because they were depressed.[1] Profits, therefore, are not a thing that the wage-earner need fear; on the contrary, he cannot hope for any early or permanent reduction in unemployment unless they are increased.

Government policy, however, while it does not determine the amount of profits that will be placed to reserve, does materially influence it; and one of the important differences between pre-war and post-war industry is the influence of Government policy. Before the war the Government imposed a tax of only 5 or 6 per cent on profits placed to reserve; now it imposes a tax of 20 per cent and upwards. The Income and Super Tax, consistently with its general principle, makes no discrimination between profits distributed and profits put back into business. To the extent of its influence, therefore, it lessens the incentive and reduces the power to expand out of earnings. If it were practicable to exempt profits placed to reserve from Income and Super Tax, the sums that could be applied

[1] Cf. *Colwyn Committee Report*, p. 19.

to extending existing businesses out of earnings would be increased by more than a quarter. It would be a subsidy, if subsidy it should be called, which would have the maximum possible effect in stimulating enterprise, since it would be given in exact proportion to the sums that already were applied by different industries and different firms to expanding or maintaining their activities, and only where such sums were being applied.

It is not possible to estimate with any accuracy the amount of such a possible subsidy, but a rough indication may be attempted. Mr. Coates, in his evidence before the Colwyn Committee, estimated that about two-fifths of the country's savings in 1924, £194 millions, or more than double the amount of new issues for investment at home, were derived from profits that were not distributed, but reinvested in the businesses of the firms earning them. Income assessed under schedule D for 1927–28 was about £1000 millions, and the proportion which profits placed to reserve bore in the accounts of the companies analysed by the *Economist* in 1928 [1] was 20 per cent. About £200 millions may be taken, then, as the figure of profits reinvested in the businesses making them. Income Tax on most of this would be levied at the full rate of 20 per cent; shareholders whose total income entitled them to assessment at a lower rate would get no reduction or return on account of their share of these undistributed profits. Super-tax would also be levied on a part, and may be set against any reduction on the standard rate of Income Tax which some firms enjoy. Complete exemption would therefore amount to a subsidy of something like £40 millions. Of this perhaps a third would go to the type of industries that are to benefit by de-rating. The

[1] *Economist*, Jan. 19, 1929.

maximum total cost to the State, therefore, would be half as large again as the cost of de-rating; but, since the subsidy would automatically be proportioned to the capacity of each firm to expand, its possible effects in increasing permanent employment would be many times as great.

The Colwyn Committee considered the proposal to exempt profits of companies placed to reserve, and, while putting with great clarity and force the benefits that might be secured, rejected the proposal. They rejected it mainly on grounds of practicability, but partly also of equity. The objections in equity were three: (1) "It would certainly be asked why relief should be given to business savings alone, and withheld from the savings of professional men and others; (2) if relief were given to companies, it would be difficult to withhold it from private firms; and (3) the relief would mainly benefit the industries which are already in a position to put large amounts to reserve, and would thus exaggerate the disparity between the sheltered and the depressed industries" (*Report*, p. 347). These are cogent reasons, but not decisive. Professional men as a class have not suffered the same losses as industry in the depression, and have not the same contribution to make to the relief of unemployment. The second objection applies only to the proposal to confine the relief to public companies. To the third it is possible to reply that already the Government discriminates between industries—by granting protection, as, for example, to the motor industry; by subsidies, as to building, and the manufacture of beet-sugar machinery; that subsidies to prosperous industries are sound in principle, if the object is to accelerate a development which will relieve unemployment, whereas it is a waste of money

(as the £23 millions Coal Subsidy of 1925–26 was a waste of money) to give relief to industries or firms that have no chance of surviving and expanding; and that sections and firms in the depressed industries would benefit, namely, just those sections and firms that had some comparative advantage that ensured their survival and gave a secure basis for expansion.

The decision must turn, therefore, on the practicability of the proposal; and here, even if one had the temerity to oppose the technical authority of the Committee, one is faced with the awful example of witnesses, who advocated the proposal only to withdraw and retreat when the Committee put the difficulties before them. Nevertheless, the difficulties seem to turn mainly on an attempt to differentiate between reserves actually applied to extending and improving equipment, and other reserves. For the purpose of relieving unemployment, the distinction does not seem necessary; reserves against losses or capital depreciation are just as necessary to the maintenance of a business in continuous activity as reserves embodied in plant and equipment. Taken by and large, a "conservative policy" in the distribution of profits makes for regular and expanding employment, and any change that facilitates and encourages such a policy will tend to relieve unemployment. If this is a tenable position, the practical obstacles do not appear to be insuperable. Net profit is an ascertainable figure, being the present basis of assessment; profits distributed, whether by companies or private firms, are as easily ascertained and certified by auditors; it should not be impossible, therefore, to ascertain the excess of the former over the latter, for exemption from the standard rate of tax, or taxation at a different rate like "earned" income or

insurance premiums. Subsequent distributions of reserves in cash would be taxable at the standard rate, since they would deplete the capital resources of the concern like current dividends; distribution of bonus shares would not be so taxable, since they would not deplete capital resources. A shareholder might, of course, sell his bonus shares if he wanted cash; but equally he might have sold his shares, the price of which would reflect the undistributed profits, before the bonus issue; in either case the company's actual capital resources would be unaffected.

The important and serious question raised and put in the questionnaire with which the Committee confronted advocates of the proposal to exempt reserves (a questionnaire that aimed rather at exposing the difficulties than exploring the possibilities of the proposal, and suggested the kind of examination paper that aims at showing how much the examiner knows rather than discovering how much the candidate knows) was this:

> Might not the ultimate end of the allowance tend to be a revolution in the concept of a tax or income? Might it not convert the tax into one on expenditure?

Ultimate ends are seldom reached in English politics; and the principle of the Income Tax is already subject to exceptions in the case of insurance premiums, "earned" income, co-operative society profits, and other cases. The argument that a shift from the income to the expenditure basis might imperil the principle of taxation according to "ability to pay" loses much of its force when the incidence of Estate Duties upon savings is brought into the account.

The issue is too big to be argued in an incidental

note like the present; but the loss of resilience in industry since the war, and the need of encouraging additional capital accumulation at the points at which it is found that additional capital can be effectively applied, make it a real issue that should be faced. The Treasury is not merely a tax-collecting machine; it is the organ through which the Government takes into consideration the total effects of Government policy upon national economic activity. If it is unable to reduce the brake upon industry by reducing Government expenditure, it is bound to explore all possibilities of shifting the incidence of taxation from the active to the passive elements in economic life. It is bound to do so the more as a corollary of deflation, which involved a transfer of wealth in the opposite direction, from the active to the passive elements. Taxation and trade depression constitute a vicious circle. Taxation is increased to meet the distress caused by depression, and recovery is delayed by the weight of taxation. Expediency, if not justice, would point to an arrangement of taxes that put the cost of relieving unemployment caused by the war upon the community as a whole, and relieved industry at the points at which recovery is taking place. In fact, by putting the cost of unemployment relief upon a so-called "Insurance Fund", maintained by levies upon firms proportioned to the amount of employment they give, and, so far as this was inadequate, upon local rates, the greater part of the cost has been added to the costs of industry; while any profits that were available for assisting recovery were simultaneously taxed. Taxing employment to subsidise unemployment, and the resources of enterprise to relieve *rentes* and salaries, and we wonder that recovery is delayed.

CHAPTER VI

SUMMARY AND CONCLUSIONS

I. *Summary*

OUR survey of the course of employment revealed a country saddled with a problem different in kind from the unemployment of the fifty years before 1914. One effect of the war, it is true, was to exaggerate the industrial fluctuations of which, in kind if not in degree, we had pre-war experience, to produce an unprecedented boom and an unprecedented depression; but the depression was further enhanced and prolonged by the more lasting influences of the war. By stimulating an expansion of munitions industries beyond any possible need of normal peace demands, the war drew hundreds of thousands of workers into a blind alley; by checking for six or eight years the normal and necessary adjustment to changing market and technical conditions, it left certain industries to face at once a reduction in demand for their products which would normally have been spread over these six or eight years; and by dislocating the normal relation of costs and selling prices, it made it difficult not only for these depressed and swollen industries, but even for industries that were not under these disabilities, to maintain themselves in competition with the industries of other countries.

We found also that the violence of the initial collapse after the boom was associated with, and in part caused by, the monetary policy of the Government, and that the final stage in the restoration of the Gold Standard in 1925 checked a recovery which had lifted industry some way out of the extreme depression of 1922. But that recovery had been in part due to the transient influence of difficulties that handicapped German competition, and there were sufficient reasons to produce a prolonged depression after the boom of 1919–20, even if the Government had not been under the necessity of restoring the Gold Standard. The abnormal and disturbing feature of the post-war depression is not only its depth—the persistence of 7 or 8 per cent of unemployment in excess of average pre-war experience—but the delay in recovery, once the slump had come. Before the war, in Professor Wesley Mitchell's phrase, prosperity bred the crisis that led to depression, and depression produced of itself the conditions that restored prosperity. Since the war prosperity has bred crisis and depression, and depression has given way to improvement to a point, but only to a point. Even after full allowance is made for the effects of the general strike and the coal lock-out in 1926, industry shows no net recovery since 1924; more people are in employment, but not so many more as have entered industry.

The depression, while by no means confined to them, is concentrated upon the older and larger export industries. They suffered most from the unhealthy stimulus and check to adjustment imposed by the war; their costs and prices were dislocated by the restoration of the Gold Standard. The industries working for the home market, and protected in one way or another

from foreign competition, were able to keep up their charges (partly at the expense of the export industries), and so to cover costs which had not been adjusted to the world level of gold prices; the export industries had to bring down their prices to world level, while their costs remained on the inflated paper level at which they rested when the last stage in restoring the Gold Standard was reached.

Even this handicap they might have overcome if their chief competitors, the export industries of our continental neighbours, had not derived as much assistance from inflation as ours suffered handicap from deflation. Their indebtedness was reduced to a fifth or less of its real burden, or wiped out altogether; they were enabled to re-equip and reorganise out of profits made at the expense of their fellow-countrymen; and their costs, reduced relatively to prices by the process of inflation, were stabilised at this favourable level by the stabilisation of their currencies at or near the peak of inflation.

There has been a substantial reduction, we found, in the course of the years of depression, in the amount of unemployment in this export group of industries; but it has been effected, not by an expansion in the numbers employed, but by a contraction in the numbers seeking employment in them. Moreover, much of the employment that they still give is given at a loss, and rests, therefore, upon a precarious and uncertain tenure. They can no longer make the contribution which they made before the war, and which the country still requires of them, to the maintenance of the country's population; hence they cause unemployment in the industries that rely on them to provide a market, and, being highly localised, involve whole towns, districts,

and counties in almost universal depression. The expansion of industrial activity in new directions has taken up some of the displaced workers, but does not, so far, promise more than an inadequate and temporary alleviation. The expansion is due very largely to subsidies—the housing subsidies alone accounting directly and indirectly for the employment of close upon 200,000 additional workers in five years—or to Protection, which merely diverts, without adding to the aggregate of employment; some of the expanding industries are working for a satiable demand, which may be expected to reach satiation in a very few years; and some, like the biggest of all, retail distribution, on their recent scale of staff and expenses, must be regarded as to some extent parasitic, profiting by lowered wholesale prices and restricting by high retail prices the expansion of demand for industry's products. The further expansion of new industries and the recovery of old industries are alike checked by a system of national finance that applies to debt service and social services a large part of the profits out of which expansion might be fed.

If, then, nothing can be done to restore the prosperity of the export industries, or, alternatively, no developments external to British industry come to its relief, we have to look for a continued divergence between the fortunes of the sheltered, subsidised, protected industries and those of the export industries on which large parts of the country still depend, the former maintaining wages, employment, and profits at the expense in part of the latter, the latter steadily contracting, until they are restricted to those special branches and varieties of production in which the comparative advantages of this country are so great

that foreign competition is of no account. Beyond that point the divergence cannot persist; for the sheltered industries are dependent on the export group for so large a part of their market that its continued contraction must ultimately react upon them. They will be forced to prey upon one another and to bring down their prices and costs, until a new equilibrium between the different industries of the country is established, on a basis of wages and profits that bear a more uniform relation to skill, responsibility, and risk. But this new basis may very well be also a lower general standard of life, since the pre-war standard of life was made possible only by the efficiency and size of the export industries.

That is the prospect on the assumptions stated; but these assumptions need examination. Can nothing be done to revive the depressed industries? Are there no developments in prospect that would ease the task of restoration? Or, relating the question to our analysis of the trade cycle, which shows that the only cure for depression is a reduction in costs or a rise in prices, is there no means of further reducing costs? or prospect of higher prices? We will take the latter question first.

II. *The Prospects of Unaided Recovery*

Certain features in the prospect permit a hope of unaided recovery for which there was no warrant in the retrospect. We found that employment had not materially improved in the last five years, and that costs and prices were still out of relation. Looking forward, however, it is not unreasonable to hope that the costs, and therefore prices, of foreign competitors will rise nearer to the level of ours. Such a result would

be a natural though deferred result of stabilisation of prices at an inflated level; wages and other charges, which had lagged behind prices in the upward movement, will tend to continue to rise when the rise in commodity prices is checked. That is what has happened in Germany; in 1924, when the currency was stabilised, wages were only 20 to 35 per cent above the pre-war level, by 1928 they had risen to 40 to 50 per cent above. Before building too much on this prospect, however, it is well to realise that France, Belgium, and Italy have not strongly organised trade union movements, in a position to compel an adjustment of wages, like the German trade union movement; it is, moreover, precisely for such a natural deferred result of stabilisation of prices that this country's industry has for three years been waiting in vain. Prices were placed on a gold basis in 1925, but costs are still on the 1924 paper basis. There is a further consideration; French and Belgian prices are below world level, ours above; the gap to be covered is a wide one. The world's return to the Gold Standard was not a simultaneous return to a single price-level which automatically re-established pre-war cost parities, but a piecemeal re-establishment of gold currencies upon a variety of price and cost levels. And the competitive strength of continental industry is not based solely on wages relatively low through inflation, but on the technical and commercial efficiency brought about by re-equipment and re-organisation out of the profits of inflation and reparation payments.

The other factor that may ease the problem is the prospective decline in the number of persons entering industry. The Colwyn Committee (Appendix XXI.) estimated, on the assumptions that the death-rate

would be the same as in recent years, emigration at the average rate of 1921–25, and the proportion of "occupied" (*i.e.* employed or available for employment) to total population the same as in the Census Year 1921, that the annual increase in the population to be employed would be as in column A of the following:

	A.	B.
1926–31 . . .	121,000	144,000
1931–36 . . .	34,000	58,000
1936–41 . . .	7,000	34,000

On the assumption that emigration would be at the average rate of 1871–1921, the increase would be as in column B.

This prospective amelioration of the employment problem requires qualification however. Certain industries are dependent rather on the number than the wealth of the population, and, if the rate of increase in numbers diminishes, their expansion is likely to be checked. The housing and house equipment industries are in this class, and they are also among the industries which have contributed most by their recent expansion to relieve unemployment. Just as before the war the increase in the population entering industry found employment in producing goods and services for the increase in the population, so a reduction in the numbers entering industry in the next decade will involve a reduction in the demand for some goods and services. The contribution, then, that this decreased entry to industry can make is limited to easing the pressure of new labour on the market, and so increasing the chances of employment for labour already in the market. We saw that since 1924 insured industry had been unable to supply openings for all the new people entering it, without making any impression on

the mass of war-induced unemployment; in the 'thirties, it should be able to meet the former need and so ease the latter. On the other hand, the shortage of juvenile labour may increase costs by compelling the employment of adults at work hitherto done by juveniles.

Whatever the prospects of an easing of the problem of unemployment by changes outside British industry, it would be bad policy to wait for these to solve the problem. Industry is not static; it cannot expect to maintain its efficiency if it is making losses, still less to improve it. Nor are the moral effects of waiting on outside help less doubtful than the material; neither labour nor management is stimulated to greater efforts by a continuance of unrelieved depression year after year. If, therefore, the hope that external conditions will become more favourable is reasonable, it is an argument rather for temporary measures designed to maintain the morale of industry than for doing nothing; whether those temporary measures take the form of providing work by an expansion of public enterprise, as Mr. Lloyd George proposes, or of carefully devised educational and remedial training adapted to the needs of different classes of unemployed persons, as Mr. Davison proposes, or both, is irrelevant to the present discussion.

III. *Can Costs be Reduced?*

Let us turn to the other question: Can nothing be done to restore the depressed industries? or, to put the question more concretely, is it not possible to reduce costs, and so restore a margin of profit on which enterprise could revive, even at the present level of selling

prices? It should be observed that it is not necessarily a criticism of the managements of the depressed industries to point out that their costs are too high. They are too high, because the prices by reference to which they are too high have been forced down by circumstances outside industry's control. All that pre-war experience would suggest may have been done; and there is no ground for the assumption commonly made that the cotton industry, that still secures a half of the total world export trade in cotton manufactures, or the shipbuilding industry, that still builds half the world's new tonnage, merely because they are depressed, are less efficient than more prosperous industries, which are not exposed to foreign competition and have not demonstrated their efficiency against competition in the export field. The inference that it is fair to draw is that the post-war problem cannot be solved by pre-war expedients. Something more than the economies that sufficed to restore activity in a pre-war depression is needed now. The changes in the competitive position that the war at once brought about and concealed have to be faced, and the adjustment to them that the war deferred completed.

Let us review again the costs that have either risen disproportionately, or not fallen proportionately, in relation to commodity prices. The first and most important is wage-rates. Before the war the policy of maintaining wage-rates in spite of unemployment could be practised only by the organised minority of wage-earners. The majority were unable to resist reductions that were needed to maintain employment; and any workers excluded by the policy of the stronger unions could compete for employment in industries in which wages were not held above absorption level.

To-day there are no unorganised industries in this sense; wages are held up generally, either by trade union or Government support through statutory wages boards, and workers excluded from employment by a *general* holding up of wage-rates above absorption level have no resort except unemployment relief. Before the war, again, in the absence of any general unemployment relief, it was impossible to maintain wage-rates generally at a level that restricted employment throughout industry; somewhere, usually at many points, wages (in relation to efficiency) would be reduced to the level at which expansion could take place; the condition "in relation to efficiency" is necessary, because, in fact, expansion took place in the high-wage rather than the low-wage industries. To-day trade union negotiators can afford to take the risk that a wage-rate on which they insist will cause unemployment, because their constituents will be provided for by the national relief scheme.

Even if the union negotiators were under the same compelling incentive to take account of unemployment as they were before the war, there are factors in the wage situation that would lead them to resist reductions. Wage-rates already are lowest by pre-war standards in the industries suffering most from unemployment, and highest in the industries suffering least. To ask miners, steel workers or skilled engineers to accept further reductions, when already their rates are below those of lower grades of skill in sheltered industries, is to invite opposition. Moreover, reductions have been tried in some cases, only apparently to make things worse; the experience of the coal-mining industry, in which an extension of hours and reduction of wage-rates led, not to employment and prosperity,

but to a further contraction of employment and further losses, made a deep impression upon workers in other industries, who did not consider whether the demand for their products was as inelastic as that for coal.

On a sectional view of their interests the workers are probably right; there is no stimulus to employment to be gained from a reduction in wage-rates in a single section of industry. Only a concerted and co-ordinated revision of all wage-rates, which would bring down indirect labour costs, would afford any great stimulus to employment; and for such co-ordinated action there is no machinery. Revision would be economical only if it were made by consent, and consent is not likely to be secured so long as wage-earners fear that any concession on their part will be used merely to increase the profits, or reduce the losses, of loan-holders, banks, the distributing trades, and sectional interests that contrive to earn profits in spite of industry's losses. Wage revision therefore offers little chance of reducing costs, unless it is undertaken as part of a general reorganisation in which other parties in industry contribute equivalent sacrifices.[1]

A rate of wages is not, however, the only cost, or even in all cases the chief cost, that a trade union can impose upon industry. Unions seek to secure their members' interests in any change that might affect wages, and, since they exercise their influence from outside, they sometimes pursue this object by obstructing or delaying change. They still restrict entry to skilled trades by limiting the number of apprentices, as in some branches of the printing industry, impose

[1] On wages and unemployment cf. "The Public Regulation of Wages", by the present writer, *Economic Journal*, Sept. 1929, and *The Problem of Industrial Relations*, ch. iv. and v., by the present writer.

restrictions upon the use of new machinery or—what comes to the same thing—refuse to make the concessions from ordinary practice that are needed to make the introduction of new machinery worth while. Their consent is, therefore, needed to any drastic reorganisation of industry, if it is not to involve friction that is expensive. The Mond Conference interim reports are evidence that this consent can be secured, on condition that the unions are taken into consultation in introducing changes; but the experience of the war, when the union leaders approved of dilution and the rank and file steadily obstructed it,[1] is less promising. An American precedent is suggestive. The Amalgamated Men's Clothing Workers in 1922, faced with a demand for a further reduction in wage-rates, refused to concede a reduction, but undertook instead to assist the employers in reducing labour costs. They virtually made themselves responsible for reducing costs at least to the level of costs of non-union employers, and, in discharge of that responsibility, have since then purged the industry of restrictive practices and established and insisted on standards of output, supported by systems of payment by results, much more effectively than any employer could have done. In the present condition of British industry, labour is faced with the same alternative; either labour costs must be reduced by lowering wage-rates, or in some other way. In any reorganisation of industry an attempt should be made to induce the union leaders, as some of them are anxious to do, to assume responsibility for reducing labour costs; and this, not by attempting to instruct the employer in the proper method of equipping and managing his business,

[1] Cf. *Problem of Industrial Relations*, ch. ii., "Government Control of Wages in War Time".

necessary as that may sometimes appear, but by dealing faithfully with their own members and eliminating from industry all practices restrictive of output and obstructive of reorganisation.

The addition to labour costs represented by employers' contributions to national insurance funds and local rates are almost as inelastic as wage-rates, though for different reasons. It is probably politically impossible to reduce the rates of benefit; yet these were placed on their present level in the period of high prices after the war, so that the maintenance of them, now that the cost of living has fallen by two-fifths, is equivalent to increasing them. If they were appropriate when they were fixed, they are extravagant now; the more so, since industry, which was prosperous and active then, is depressed and under-employed now. If, however, it is politically impossible to change the rates of benefit, it should not be necessary to finance them by a tax on employment. As we have seen, the more people a firm employs, the greater it has to pay towards the maintenance of the unemployed and towards the provision of sickness insurance benefits. So far as unemployment is a normal incident of industrial life, it may fairly be relieved by a tax on employment; but post-war unemployment is, to the extent of at least two-thirds of its volume, an abnormal industrial phenomenon, directly attributable to the war, and as much a war expense as the expenditure represented by the National Debt. Similarly, the provision of income in sickness, old age, and widowhood may properly be met by insurance contributions levied on wages, since insurance is simply a device for securing a better distribution in time of the income on which a man has to live, whatever its source and amount; but there is no

economic justification, when industry is already paying wages at rates that make it impossible to give full employment, for imposing an additional charge, never taken into account in varying wage-rates, to meet expenditure that was formerly met out of wages. If wage-rates cannot be reduced to compensate the employer for the increased burden of insurance contributions, either benefits should be reduced in proportion to the fall in the cost of living and the saving used to relieve the employer, or Parliament, if it wishes to maintain benefits at their higher real rate, should provide the whole cost in excess of the wage-earner's own contribution out of the proceeds of general taxation. It is not possible for competitive industry to maintain employment at enhanced real wage rates and pay increased insurance contributions out of a diminished net revenue.

The burden that local rates impose has—in the eighth year of the depression—been recognised by the de-rating scheme of the present Government. The method of relief adopted, however—a uniform proportionate reduction of rates—does not take account of the incidence of the cost of relief. Concentrated upon areas in which rates were high, because localised industries were depressed and poverty intensified, it would not only have improved the depressed industries' chances of recovery, but would have offered an inducement to new and expanding industries to settle in these areas. As it is, if Essex was more attractive than Durham or Glamorgan because of lower rates before the change, it remains more attractive in the same proportion, although the absolute amount of the burden has been reduced; and the need remains of transferring surplus population from the areas of contracting

industries, with all the loss involved in leaving these districts derelict, instead of attempting to assist and stimulate enterprise where the surplus population is.

The burden of social services and local rates may seem to have been exaggerated. The Balfour Committee in its Final Report observes of them that "the most important consideration is not the direct money cost of social services, but their effects upon industrial efficiency. . . . The sense of security and the relief from suffering thus obtained is a national and personal asset of the highest value, which is often neglected in making comparisons of British wages and conditions of labour with those obtaining in other countries".[1] This is true; but the beneficial effects of the provision are due to the redistribution of available income that it secures to neglected points of urgent need; if it reduces available income by its effect upon costs—and, as the Committee imply, no account of it is ever taken in fixing the rates of wages to which these services are an addition—there will be an offset to put against the benefits. Employers' contributions were estimated by the Committee at £50 millions a year, rates at another £35 to £40 millions, the resulting charge on costs being less on the average than 1 per cent of the value of gross output. But this is another case in which averages are misleading. The burden varies from industry to industry, amounting in the case of the export industries to between 2 and 3 per cent of total cost, or between 7 and 10 per cent of the wages bill. Even after de-rating, and assuming no increase in rates, it will still represent an addition of from 4½ to 6½ per cent to the wages bill.

Nor does this figure indicate the possible effects upon employment. Industry is not carried on by firms

[1] Final Report, pp. 257-258.

equal in resources and efficiency, incurring identical costs and securing equivalent results, but by firms of varying efficiency, some making profits and some losses, and all probably doing different portions of their output at different rates of profit or loss. If we had the necessary particulars, we could arrange the output of an industry in a series, the different amounts being graded according to the costs of putting them on the market. We should then see that the price level intersected our series, dividing it into a part that paid, because the price covered the cost, and a part that was produced at a loss; and anything that reduced costs, assuming prices were unchanged, would lift a portion of the output on which a loss was being made into the paying zone. Even if competition forced producers to transfer the savings on costs to the consumer in lower prices, the increase in volume sold, consequent upon lower prices, might make it possible to reduce costs in other ways, and so increase the proportion of paying production. A memorandum prepared by Dr. W. H. Coates for the Colwyn Committee gives some indication of this grading of output by costs in a number of representative firms; the following table is derived from it:[1]

TABLE VII

PERCENTAGE OF TURNOVER, DONE AT INDICATED LOSS OR PROFIT, BY CERTAIN FIRMS

Loss (−) or Profit (+).	Cotton.	Wool.	Iron and Steel.	Metal.	Food.	Wholesale Distribution.	All (including Retail Distribution).
−4·9 to 0%	16·15	6·09	5·04	15·54	10·17	9·03	8·0%
0 to 1·9%	15·78	5·0	2·64	9·19	15·21	32·95	18·1%

Thus a 5 per cent reduction in costs would have

[1] Colwyn Committee's Report, vol. II., Appendices, p. 94.

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brought 16 per cent of the production in the cotton manufacturing firms, at present done at a loss, into the payable zone, and nearly 9 per cent of the turnover of all the firms; on the other hand, an increase of 2 per cent on turnover in costs would depress nearly 16 per cent of the cotton turnover below the paying level and 15 per cent of the turnover of all the firms. These figures refer to the year 1922–23; since then prices have fallen, rates have risen, employers' contributions to insurance funds have risen. The effect, therefore, of flat-rate increases in costs, imposed indifferently on prosperous and unprosperous firms, like rates and insurance contributions, is to be judged not by their relation to costs as a whole, but by their influence upon the marginal output of marginal firms. A small proportionate increase in costs may cause a disproportionate contraction in output and employment, by making it impossible for some firms to continue producing at their previous rate and for others to carry on at all; contrariwise, a small reduction in costs may make possible an increase in production so great that the aggregate return that the industry can make to the parties conceding the reduction is actually increased.

We come to the element in costs represented by indebtedness, on which interest charges have to be paid whether they are earned or not. The expansion of nominal ordinary capital that took place in the post-war boom does not affect costs, since the holders of ordinary shares are not entitled to dividends unless there are profits available for distribution; but the increase of indebtedness that went with it, due partly to the desire to expand while business was profitable, and partly to the need of additional resources to finance, at the high level of prices then ruling, purchases

of raw materials and uncompleted contracts, is bound to affect the price policy of firms. Either they will refuse business at prices that will not enable them to cover these debt charges; or they will cut prices in the endeavour to secure current receipts, even at a loss, to pay their debt charges, and so sink into insolvency. In either case, sooner or later, employment is contracted. The fall in prices since 1920 has increased the real burden of this indebtedness, since it compels the indebted firms to pay interest in pounds of higher value; the cotton-spinning industry of Lancashire, for example, borrowed perhaps £30 millions in 1919–20 at an average price level of 240, in other words, when pounds were equivalent to 8s. 6d. each in pre-war money; it is paying interest on most of this debt with the price level at 140, in pounds which are the equivalent of 14s. 6d. each in pre-war money.

This indebtedness is partly funded in debentures and bonds; more perhaps in indebtedness to the banks.[1] Where the amount of indebtedness is considerable it is a serious handicap in competition with countries whose debts have been scaled down or wiped out by inflation. It has other inconveniences; as we have seen, it is idle to approach labour for a concession on wage-rates, where the whole concession would merely be swallowed up in interest charges paid to *rentiers* or bankers, to whom the fall in prices has already transferred an increased proportion of the product of industry; and it makes it difficult, if not impossible, to raise new capital for necessary re-equipment.

[1] The 1709 joint-stock companies (not all of them operating at home), the accounts of which were analysed by the *Economist* in 1928, showed the following distribution of capital under different heads:

Debenture Capital.	Preference Capital.	Ordinary Capital.
£98,218,072	£112,329,637	£215,896,368

Industries that are profitable will in course of time rid themselves of their handicap by paying off their debts; but industries that can do this contribute only indirectly to unemployment. For the depressed industries the only alternatives are liquidation by inducing their creditors to accept a writing down of indebtedness, and a further contraction by bankruptcy. The situation eight years after the depression began is much more serious than it should have been, because the banks, with an ill-timed generosity, have kept in existence large numbers of firms that were really insolvent in the changed commercial conditions. Perhaps the banks were influenced by the speeches of their chairmen, which, with a unanimity that became depressing, prophesied annually a trade improvement that, if the merely seasonal improvement that marks the first four months of the year is allowed for, never materialised. Whatever the explanation, an important element in bringing about trade recovery in pre-war depression, the elimination by bankruptcy of the less efficient or well-placed firms, has not been allowed to operate in the post-war depression with its pre-war force, although the need of concentrating production under the more efficient managements was more urgent than ever before. Another way in which these insolvent firms have delayed recovery is by "weak selling", depressing prices below the level which the consumer would pay without contracting his purchases, and so dragging down solvent firms with them. The coal and cotton industries owe a good deal of their exceptional depression to reductions of prices, that brought with them no compensating expansion of sales, due to the desperate price-cutting of firms that are really insolvent.

In the light of this review of costs, it is not difficult to understand the recurrence of appeals for some form of inflation. Inflation would raise prices and revive confidence. It would be unnecessary, at first at any rate, to raise wage-rates, since they were not generally lowered when prices fell after 1924; and insurance contributions, interest charges and other fixed charges would all be relatively lighter. In a word, the dislocation of costs and prices which deflation caused would be automatically set right. Unfortunately for proposals of this order, they are impracticable so long as the country stays on the Gold Standard. It is not possible to increase the note circulation without securing more gold. The methods of inflation still open—lowering Bank Rate and purchasing securities in the open market—would probably have no effect in the present condition of industry, which is troubled with no lack of liquid resources. If, however, they did lead to a rise in prices in this country, gold would tend to leave the country, and the Bank would have to choose between reversing its policy, in order to attract gold back again, and letting the Gold Standard go.

It is improbable that the country would consider the latter alternative, involving as it would the severing of the link between British currency and other countries' currencies which has been restored with so much pain, and the restoration of all the uncertainty that comes from the mere possibility of Government interference with the amount of currency. But, if the persistence of depression compelled it to consider the alternative, there are factors that would compel it to reject it. London would tend to lose the foreign balances, which make its credit conditions relatively easy, if it forsook the Gold Standard. The reduced

value of sterling, due to the fall in the exchanges that would result from a rise in the British price level, would reduce the value of all securities held by Englishmen abroad, the interest on which is fixed and payable in sterling. It would increase the money cost of imports, particularly imports of raw material and food, and so, before long, lead to demands for increases in wages, which would neutralise part of the advantages of inflation. The refusal of such advances, or even the spectacle of expanding profits, would provoke the same discontent and outbreak of strikes as rising prices brought in 1919 and 1920.

Inflation is not a practicable policy. It was rejected, when the decision to return to the Gold Standard was made in 1919 and 1925. There is no alternative left except to complete the process of price readjustment initiated then and inevitably involved in deflation. The task may be eased by a rise in costs in competing countries; but it would be unwise to wait for that. On the other hand, our survey of costs has shown them to be rigid and inelastic. We are left with the necessity not only of reducing costs on an unprecedented scale, but of finding some new way in which to effect the reduction.

IV. *Rationalisation*

Such a new way is offered by rationalisation. Whether under that description or some synonym, all the inquiries, official and unofficial, that have reported on the plight of British industry since the war, put forward what is in effect the same prescription. A general reorganisation, in which past losses and debts will be written off and by which costs will be reduced, is declared to be essential.

Thus the Liberal Industrial Inquiry, the most elaborate unofficial survey of post-war industry, stressed the lack of any organisation of industries as units as the chief factor explaining the inability of the depressed industries to cope with the changed post-war situation. England was contrasted with Germany and America in its "obstinate prejudice to what is called rationalisation", and the possibilities of reducing costs "merely by rational conduct of the industry as a whole", illustrated by the cases of coal, steel and corn milling.[1] The two latter illustrations may be quoted:

> The cost of rolling steel depends on the quantity of any given section that can be rolled. If an agreement could be made to distribute the orders among the different works in such a way that each would have the most continuous possible work on the smallest varieties of sections, there would be a substantial saving. It simply means organising the industry for mass production. It is understood that proposals of this sort have been before the industry for ten years, and that everyone agrees in principle that this should be done and that great economies would result. No steps, however, seem likely to be taken.
>
> Our third illustration is from the fairly prosperous industry of flour milling. Here we have an over-production estimated at about 30 per cent, with big mills in the various ports sending their flour to all parts of the country with serious overlapping, and therefore with heavy unnecessary charges for salesmen and for transit. In this case most of the mills are highly efficient, and only slight economies would be practicable. But big economies are certainly possible if the worst situated and equipped mills are closed down and the production concentrated on the best. Here again it is agreed by everybody in the industry that big savings could be effected in this way, but in no other way, yet nothing is done.

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[1] *Britain's Industrial Future*, pp. 42-43, 127-135.

The Final Report of the Balfour Committee is more explicit:[1]

The main practical problem which emerges from all our inquiries is a perfectly plain one, viz. to find the means of restoring the competitive power of British industry and trade without impairing the standard of living, and of enabling British exporters to place their products in external markets in sufficient volume on terms acceptable to overseas buyers.

It is, we think, abundantly clear from our survey that the first step towards putting British industries in a position to compete successfully in overseas markets is to subject their organisation and equipment to a thorough process of reconditioning. To carry through this process successfully, two prerequisites must be fulfilled. In the first place, there must be an active *will* to reorganise, based on real insight into the changing conditions and needs of the national and international economic situation. In the second place, there must be the *power* to reorganise, based on adequate means of access to the financial and technical resources necessary for material equipment, together with the whole-hearted co-operation of all the human factors to ensure that the best results shall be obtained from the transformation. . . .

It has been made plain in the preceding pages that the reconditioning of British industry will undoubtedly involve a great deal of scrapping and replacement of plant, and enlargement of the industrial unit, both by growth and by the regrouping of units through consolidation or other forms of association, so as to obtain the full benefits of large-scale production, elimination of waste, standardisation and simplification of practice, and all the other measures of economy usually included under the comprehensive term of "rationalisation".

The Treasury reply to Mr. Lloyd George and Mr. Keynes is equally definite, in a passage the first part of which those gentlemen would doubtless endorse:[2]

[1] P. 297.

[2] Cmd. 3331, p. 52.

The ultimate remedy for unemployment is not to be found in such measures. It must be solved by reducing the costs of production and the cost of living. There was a time perhaps when reduction of the costs of production was looked upon as largely synonymous with reduction of wages. In present conditions it must be sought in the improved organisation and efficiency of all the elements of industry, in the adjustment of the businesses of the country to the changes that have taken place in world demands and in the supplies from different countries, in the improvement of our selling methods and in all that is implied in the term "rationalisation". In the meanwhile the procedure proposed in the pamphlet tends to encourage British industry and labour in false hopes, and thereby prevents the steps from being taken which would lead to recovery.

Even more significant, perhaps, are the conclusions of investigators into particular industries. The coal-mining industry has been much inquired into. The Samuel Commission's view of its needs are indicated in the following extracts from the Summary of Findings and Recommendations:[1]

The amalgamation of many of the present small units of production is both desirable and practicable. This may often be effected from within, but in many cases it will only take place if outside assistance is given. . . . The State as mineral owner will be able to promote desirable amalgamations when granting new leases or renewing old ones. Legislation should provide for a compulsory transfer of interests under existing leases where desirable amalgamations are prevented by the dissent of some of the parties or their unreasonable claims. . . . A closer connection of mining with the allied industries should be promoted. . . .

The industry as a whole has so far failed to realise the benefits to be obtained by a readiness to co-operate. Large financial advantages might be gained by the formation, in particular, of co-operative selling agencies. They are specially needed in the export trade.

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[1] Cmd. 2600, pp. 233-234.

The earlier (Sankey) Commission went further, and recommended complete unification under a form of national ownership.

The Lancashire cotton industry has been the field of almost continuous reconstruction discussions. The American Yarn Association, the latest and most effective of the organisations formed to deal with its problems, after experimenting with output and price control, finally evolved a scheme for the voluntary merger of as many of the firms in the industry as were prepared to enter. The basis was a valuation of the assets of each firm applying, and the satisfaction of all claims, whether of creditors or shareholders, by an allotment of income bonds or shares in a new company, the Lancashire Cotton Corporation. Economies were anticipated, a reasonable estimate of which was possible, from centralised buying and selling, standardisation of products and the concentration of separate mills on separate products, as well as from a reduction of the burden of loan and interest charges, and the improvement in equipment which new capital, that was promised the new corporation, would enable it to instal.

Such unanimity is perhaps a little suspicious. It suggests that the investigators, being unable to find a solution of their problem in any of the detail modifications and adjustments that industry could make without extensive reorganisation, put forward the fashionable nostrum, not from conviction, but, *faute de mieux*, because it had not been tried and therefore could not be refuted. That is a possibility; but it is also possible, and more probable, that such unanimity is significant of the real nature of the problem. Ordinary remedies have not served, something unprecedented is called for. Recovery will come, from post-war as from pre-

war depression, only when costs are got below receipts, and pre-war methods of reducing costs are inadequate. The unanimity of these diverse inquiries is consistent with the evidence of our own analysis of post-war unemployment—that it has a specific war-induced element which was not present in pre-war depression and will not yield to pre-war treatment. If all inquirers, who have faced the facts, have found themselves compelled to put forward a novel and untried remedy, it may very well be that the chief need of British industry is to get away from pre-war ways of thinking and handling the problems of industry, and recognise that the post-war world is a new and different world.

Rationalisation is not merely a "blessed word". If it is sometimes used as a substitute for thought, it is also a convenient term of reference to describe certain well-understood devices. Briefly, it implies industrial combination with the object of securing not monopoly prices, but certain productive economies. The economies are due mainly to the possibilities that combination usually offers of a more economic division of functions. In particular, financial control and technical control can be separated; because the right technical unit is not necessarily the right financial unit. But there are other potential economies. Much duplication of staff and waste of energy are involved in buying materials and selling products, when a number of firms engaged on the same products in the same locality for the same markets each maintains its own buyers and selling agents. Research and other expert services are likely under the same circumstances to be both duplicated and starved. An uneconomic diversification of product will be attempted in every plant, when economy requires specialisation of each plant to

the narrowest range of product that will keep it fully occupied. Diversification of product is no doubt desirable as a method of spreading commercial risks, utilising more intensively a sales organisation, and securing generally a bigger return from a given expenditure on overheads; but it is economical only if the scale of the concern practising it is large enough to combine it with bulk production of all the chief classes of output. These economies, it may be said, are potential only, and may not be realised; but what equivalent economies are offered by any alternative scheme of dealing with costs?

Nor is rationalisation anything new. The textile finishing trades were "rationalised" at the beginning of the century, and have demonstrated the virtues of such reorganisation by their relative success in the depression. Cotton thread is an older instance, cement a more recent one. It is not necessary to look to Germany or America for examples of the advantages of organising and operating an industry as a single financial unit. The classic analysis of the economies of such a method was made in England as long ago as 1907.[1] Nor need the combination be an inclusive monopoly; the economies sought are attainable by grouping, which falls short even of a national monopoly, as these instances show.

For two reasons that were not operative before the war, reorganisation on these lines is a necessity of the depressed industries in the position in which they find themselves after the war. They are burdened with debts to debenture holders and banks, which handicap them in competition with continental competitors, who were relieved of corresponding burdens by in-

[1] *Industrial Combination*, by D. H. Macgregor.

flation and stabilisation of prices at the high level established by inflation. And they suffer from inferiority of equipment by comparison with the same competitors, who were able, out of the profits of inflation and the compensation they received for war losses, to re-equip their plants with the most modern machines and lay-out. Before the war the equipment of British industry, even if it was not always up-to-date, was at least competitive. Most firms made profits, trade had been good for the four years before the war, and a large part of the profits made had been put back into industry in the form of new and additional equipment. The check to profit-earning since 1920 has checked also this process. The industries that need re-equipment most are the industries least able to afford such re-equipment out of their own resources. They are forced to apply to the capital market, by public issues, for any considerable capital expenditure, and they can hope to make a successful application only if they can first reduce the indebtedness which at present absorbs the greater part of trading profit. They are in a vicious circle; indebtedness can be discharged only if they can earn larger profits; larger profits can be earned only if they can re-equip; and capital for re-equipment cannot be secured unless their indebtedness is liquidated.

Rationalisation offers a prospect of breaking this vicious circle. The creditors of the depressed industries are interested in restoring them to activity, because their security diminishes the longer depression persists. They may, therefore, reasonably be asked to accept some reduction in their legal claims, on condition that the reduction is part of a reorganisation that will increase the security for what is left of their

claims. Since in effect the only security is the earning capacity of the industry, if new capital is needed to restore earning capacity, they have no alternative to agreeing to a reduction. A great many financial reconstructions of individual firms, involving large concessions from the holders of the prior obligations of the firms, have been carried through on this basis. The prospects of restoring earning capacity, and of lifting firms in the depressed industries out of their present condition, will be very much increased, if the reorganisation takes the form of combination as well as financial reconstruction. It is possible in such cases to offer creditors some compensation for the reduction in their fixed claims; they can be offered a share in the residual profits of the industry, which will be worth something, because the chances of earning profits and resuming expansion will be increased by combination. The financial reorganisation, which is the only alternative to bankruptcy for many firms in the depressed industries, can be linked up with amalgamation, and any concessions by creditors made conditional upon entry into the combination on whatever terms are necessary to give the combined industry a fair chance of making profits. The problem created by the growing burden of debt thus provides the opportunity for rationalisation.

v. *The Obstacle to Rationalisation*

There is a general agreement, then, that British industry requires a large measure of reorganisation, and that the reorganisation required is that commonly referred to as rationalisation. When we proceed to ask how rationalisation is to be secured, we get no such

unanimity, and very little guidance. The Treasury, having said that reduction of costs is no longer synonymous with reduction of wages, but must be sought in "rationalisation", leaves it at that. The Liberal Industrial Inquiry makes important proposals for altering the constitution, privileges and obligations of different classes of joint-stock companies, which would be required if industry had been generally reorganised. It summarises admirably also the defects that call for rationalisation and the advantages to be gained; and insists with truth that the obstacles in the way are psychological and personal rather than material. But there it also leaves the matter. "Clearly", the section ends, in which the obstacles to reform are enumerated, "this is a matter for industry itself". "There is urgent need", the report says elsewhere, "in many of our leading industries, struggling as they now are with adversities which seem beyond their control, for some organisation of the industry as a whole which will enable it to steer a deliberate course, adapted to the conditions which it has to meet, instead of drifting helplessly before them. The particular system of organisation which circumstances render most appropriate and most feasible will vary from industry to industry; and we shall, therefore, not attempt to go further into detail. But it is vital that the need should be clearly recognised." But no suggestion is made of a course of action, if the need is not clearly recognised by industry itself, and nothing is done.

Similarly the Balfour Committee insists on an "active will" as a condition of reorganisation and recovery, points out that rationalised industry will involve "a great change in the average business man towards new ideas". Later they say, "While fully

recognising that the general economic policy of the State may contribute to ease the difficulties of the transition, we are profoundly convinced that the first steps (towards financial reconstruction) must come from the industries themselves". They do not believe "that any of our principal basic industries have been so weakened . . . as not to have the power within themselves to take the first measures towards their own regeneration, provided that they are thoroughly convinced that such measures are essential and unavoidable, and that they must be taken by themselves without reliance on any outside authority". But what if the present heads of businesses, whose attitude is "the attitude of the average business man", are not convinced that reorganisation is necessary, but believe, as they have believed for the last eight years, that trade is just going to improve, and will not take the initial steps towards rehabilitation? What if the defects characterised in the Liberal Report, "a wrong tradition—individualism instead of co-operation, secretiveness instead of publicity, neglect of marketing, indifference and hostility to research"; and the "personal" difficulties—"jealousy and mistrust among people at the top of various concerns, vested interests of all kinds, the carrying on of things as they are, apathy and lack of imagination to realise the importance of reform"—persist and prevent the formation of "some organisation of the industry as a whole that will enable it to steer a deliberate course"? Can it still be contended that "clearly, this is a matter for industry itself"?

The experience of the last eight years points to the conclusion, however reluctant we may be to accept it, that industry itself has neither the will nor the power to reorganise itself. Such reconstruction as has taken

place has been forced upon individual firms by their financial difficulties, and has not, with one important exception to be referred to in a moment, resulted in any national reorganisation of a depressed industry as a whole. Where the work is highly specialised and the number of firms engaged in an industry is small, as in the case of the armament industry, financial reconstruction has suggested and been followed by technical reorganisation; a redistribution of work has been carried out, in order to concentrate each kind in plants that are specialised to it. But in most industries the number of firms has proved too great, and the disparity of fortunes and prospects too wide, for the different units to come together spontaneously.

The one case in which an industry has been organised into a unit of national scope is the heavy chemical industry. Here the number of firms to be combined, when Imperial Chemical Industries was formed, was only four. Three of these were themselves combinations, the directors of which would already have experience of the advantages of combination and an insight into the possibilities of further combination. One of these constituent combinations was formed at the end of the war in the explosives branch of the industry, and illustrates well the part that rationalisation might play in meeting depression. This branch had been expanded in greater degree by the demand for munitions than any other industry, and had to face world competition expanded by similar influences in other belligerent countries. By combining to meet the inevitable contraction in demand, and deciding for itself, instead of leaving the decision to the fortuitous action of competition, which plants should be closed and which kept in use, the industry was able to reduce

costs, explore new demands, and, after an initial reduction in scale, to resume expansion.

The chemical industry is, however, the exception, and the first and essential step towards rationalisation is the recognition that it will not come, within any period that is relevant to the present unemployment problem, by the spontaneous coming together, without pressure from outside, of the firms with whom the direction of the industries of the country rests at present. Two instances in which amalgamation and concentration offer the most favourable prospects of restoring profitable working without industry responding have been cited from the Liberal Industrial Report. The example of the coal-mining industry is even more decisive. The necessity of merging the 1400 existing units into a smaller number, in order to secure the economies of working each coal-field as a unit, concentrate production on the more efficient pits, and economise in distribution, was the chief lesson brought out by the evidence put before the 1919 Commission and embodied in both the Sankey and the Duckham reports. The Commission of 1925–26, while it did not recommend unification, laid even more stress on the importance of amalgamation of units and concentration of production and marketing, and recommended State purchase of mineral rights primarily as a means of compelling co-operation of this sort. On both occasions the mine-owners preferred to meet the situation by a reduction in wages—in the latter case by an increase also of working hours without any corresponding increase in wages. The complete failure of the policy adopted to restore prosperity has not led even now to a consideration of the alternative recommended by the two Commissions. In 1926 the Government of

the day acted on the recommendations of the Samuel Commission so far as to pass through Parliament an Act designed to promote amalgamations.[1]

The results were summed up, by a not unsympathetic observer, in the City Column of *The Times* of March 25th:

> Although more than two years have elapsed since the passing of the Mining Reorganisation Act, relatively little has been done towards the reconstruction of the coal-mining industry. The slowness to take advantage of the facilities provided by that Act is due to several causes, but none the less it is to be regretted. It is true that the coal trade has improved in recent months, but the more thoughtful colliery owner recognizes that it affords no reason for delaying or abandoning the rationalisation of this great industry. The purpose of rationalisation is to modernise the organisation of the coal trade; to raise its efficiency in production, treatment, distribution and marketing. It is therefore an economic necessity. Although amalgamation has reduced the number of individual collieries, the industry is still carried on in the main by a large number of individual

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[1] Part I. of the Act (sections 1-12) contains provisions for facilitating the reorganisation of the coal-mining industry. The first subsection of Section 1 provides that where the owners of two or more undertakings consisting of or comprising coal mines agree to amalgamate their undertakings either wholly or partially they may prepare a scheme of amalgamation and submit it to the Board of Trade; and the second subsection similarly empowers the owners of any such undertaking, or of two or more such undertakings which have agreed to amalgamate, to prepare and submit to the Board of Trade a scheme for the total or partial absorption of one or more other such undertakings which are unwilling to amalgamate or to agree to the proposed terms of amalgamation. Sections 2-5 set forth the permissible contents of such schemes, and deal with other consequential matters.

Under Section 6 the Board of Trade are to consider schemes submitted to them, and if satisfied that a prima facie case has been made out for any scheme, to refer the matter to the Railway and Canal Commission; while Section 7 provides that the Railway and Canal Commission shall hear any objections to the scheme, and thereafter may either confirm the scheme, with or without modifications, or may refuse to confirm. A scheme confirmed by the Commission becomes binding on all persons.

Section 12 empowers the Board of Trade to assist in formulating or settling the terms of an amalgamated scheme, if it appears to them that it is the general wish of the owners of any undertakings that they should do so.

concerns, each acting independently. Some are grouped together for certain purposes, but the connection is loose, and certain features of the arrangements, far from promoting efficiency, tend to reduce it. This is especially true of the large, modern, up-to-date mines which are operated by arrangement below capacity, and therefore uneconomically.

Actually by the end of 1928 the Railway and Canal Commissions had sanctioned 17 schemes, covering 172 pits which normally employed 126,000 workpeople—about a ninth of the industry—in two and a half years.

Neither the pressure of losses nor the prospect of profits suffices to induce the mine-owners to sacrifice their traditional independence. The textile industries show the same reluctance. The American section of the spinning industry has been incurring heavy losses ever since 1926; it has been obvious since 1922 that there was little prospect of the pre-war volume of output and margins of profits being attained again in this decade. Yet the directors and shareholders of firms that are unable to earn even interest charges still hesitate to accept the scheme of amalgamation offered by the Lancashire Cotton Corporation, and the banks apparently still hesitate to force them either into bankruptcy or into the amalgamation.[1]

This unwillingness or inability of industries to reorganise themselves is due in part, no doubt, to a failure even now to realise that the post-war depression cannot be relieved by pre-war expedients. But it is due also to the resistance of two classes of firms. There are, first, the successful firms, who continue to make profits

[1] One bank has now (June 10, 1929) put in a receiver in the case of two heavily indebted mills that refused to accept the terms offered by the Cotton Corporation. Great resentment is expressed at its action; but what alternative have the mills in question left it?

even in the depressed industries, either because they have some speciality, in which they are not exposed to the full force of competition, or because they are exceptionally well managed, and are content to earn less than average profits by more than average exertions. They are able to disregard the needs of their industry as a whole—for the time being; doubtless competition will spread to them and neutralise their advantages in time—and excuse themselves the labour and anxiety of attempting a reorganisation by which others will benefit most. There are, in the second place, the unsuccessful firms, which need the support of a reorganised industry if they are to be placed on a profit-earning basis again, but which can carry on for a year or two longer, by securing further assistance from complaisant bankers, or a moratorium on their existing obligations, or by a gradual depletion of capital resources in trading losses, and flatter themselves that trade may by then have recovered. Their resistance to amalgamation is not uninfluenced by the interests of directors and other salaried staff, whose stipends do not cease when a trading loss is made and shareholders go without dividends.[1] Others may have an interest in keeping a firm in existence, even when it is working at a net loss; brokers and merchants who supply it with materials, agents who handle its products on commission, customers who buy from it at prices that do not cover cost of production, even the workpeople, who get their wages even if their prospects of regular employment are diminished for the future; and all those others who may be able, as creditors, to influence the firm's policy. In such cases the development of joint-

[1] Cf. a striking letter by "A Director" on the resistance to the Lancashire Cotton Corporation published in the *Manchester Guardian* of March 19, 1929.

stock enterprise has led industry to a point at which, by separating ownership and control, it removes the incentive to economical use of capital which exists in the private firm, without securing any of the economies of scale and management which that separation makes possible.

Even when there are no such vested interests to overcome, combination in most industries is hardly likely to be brought about without some outside help. Personal jealousies, family pride, considerations of prestige lead men to resent the taking of the initiative by some other person in the industry; so that the initiative can better come from outside. And an impartial mediator is usually needed, to act as honest broker between the different firms, to assist in settling terms, and to carry through the extremely complicated negotiations involved. The organisation of industrial combinations is a specialised business with technical problems of its own, for which the manufacture of cotton, the getting of coal, or the technique of any other branch of industry gives no adequate training. The after-effects of the amateur flotations by inexperienced local company promoters in the Lancashire cotton industry in 1919 and 1920 are sufficient evidence of this.

It is living in a fool's paradise, therefore, to wait for industry to reorganise itself. Ultimately, no doubt, a new equilibrium of different industries in the community, and of costs and prices in each industry, might be reached without any organised pressure from outside industry. Indebtedness would be liquidated, and the less efficient managements weeded out, by bankruptcy; piecemeal amalgamations and the growth of the stronger firms would increase the scale of enter-

prise; production would be restricted to the volume of standard products which the better organised industries of other countries left us, and to specialities which the skill and experience of our industrial population gave us an advantage in producing. But to indicate the alternative is to condemn it. It would involve not only a persistence of the present excessive unemployment in the present depressed areas, but a further contraction of industry in these areas. The loss of capital would not be confined to the concerns that are losing money at present, but would spread to banks and other creditors that have given them credit; even if it could be confined to them, it would involve the further waste, in meeting trading losses, of capital and other assets that, if preserved, might have been used in some scheme of reorganisation. And the desperate efforts of these insolvent sellers to postpone their formal dissolution would unsettle prices and check recovery whenever demand gave the industry an opportunity of improving its position.

VI. *Agencies of Reconstruction*

Pressure from outside of some sort is necessary; compulsion, if no politer form of inducement will serve, the offer of assistance and mediation, where compulsion is not needed. What agencies are there to which we may look for the exercise of such pressure? I propose, in conclusion, to review briefly, first, the agencies in this country that have performed this function in the past; then, the agencies that perform it in other countries; and, finally, other possible agencies that might be brought into play if the needs of reorganisation have not already been met.

The one successful scheme of rationalisation that has been effected since the war, the unification of the heavy chemical industry, was due to a happy conjunction of favourable circumstances and exceptional individuals. When these are not available, the initiative may still come from within. In the Lancashire cotton spinning industry, as we have seen, an ambitious scheme has been completed and launched, and now only awaits acceptance by a sufficient number of firms to commence functioning. The initiative in this case came from an *ad hoc* organisation within the industry, formed to deal with the post-war depression. The special condition, that both explains the formation of such a body and compels the consideration of the scheme it has launched, is the peculiar financial constitution of the industry. The practice of the industry is to raise a large part of the capital needed on loan, and to call up only a small proportion of the ordinary share capital. In case of liquidation, therefore, the shareholders are liable not only to lose the whole of their investment, but to have to pay calls on the unpaid-up part of the capital if the realised assets do not cover the liabilities. Even with this unpleasant compulsion upon them, they have hesitated to accept the terms on which their properties will be merged in the new combination; and the promoters of the reorganisation would have had little hope of carrying it through if they had not been able to secure a promise of new capital on the condition that an effective combination is formed. This, it is understood, they owe to the benevolent interest in the scheme of the Bank of England.

This cotton scheme is significant as the first and largest attempt on the part of a depressed industry to reorganise itself. It meets the situation in the way that

we saw might be possible, by utilising the indebtedness of the industry as a means of bringing about reorganisation. The chief creditors, the banks, are understood to have given their approval to the scheme and to be prepared to waive a part of their prior claims, for the sake of enabling the new corporation to begin operations without charges that have to be met whether the results of trading cover them or not, and enabling it also to offer the shareholders of the most burdened firm a hope of some profits in the future. Had the banks been willing to put pressure upon firms in their debt, the scheme might have been brought into operation more rapidly; as it is, the opposition to it is still strong.[1]

In the coal-mining industry, there has been an approach to unification in the anthracite section of the industry, and some local amalgamations. But the chief efforts of the industry have been directed to controlling prices, restricting output, and recovering export markets by subsidising exports out of the proceeds of levies upon output as a whole. The result has been to handicap the more efficient firms by restricting their activities, and to keep alive less efficient firms that could not survive unrestricted competition. Such arrangements as have been made have been regional only, and have not prevented competition for the same export markets between different British fields. The Samuel Commission relied on State ownership of mineral rights as the instrument by which to assist, and, where necessary, compel amalgamation and concentration; but the Mining Industry Act of 1926 left the initiative with the mine-owners themselves. The Board

[1] Cf. the President of the Federation of Master Cotton Spinners in the *Manchester Guardian* of June 12, 1929—"drastic reforms in mill finance are being undertaken, but before this work is accomplished years will elapse".

of Trade can assist in the negotiation of amalgamations, but only on the application of parties to them; in order to enable the Board to initiate schemes it would be necessary to amend the Act.

Parliament—a different Parliament, it is true, in a different atmosphere—did not show the same reluctance to interfere with the relations of railway companies among themselves. Having decided that a merger of companies was necessary, it enacted the Railway Act of 1921, by which the existing companies were grouped into four large groups, encouraged to agree among themselves on terms of amalgamation, and subjected to a Commission, which was empowered to impose terms, if the parties could not come to any agreement without its intervention. The Commission had very little to do.

The countries in which most progress has been made in the combination of firms into larger financial units are Germany and the United States of America. In Germany the reorganisation has been facilitated by the relation of the joint-stock banks to industry. Owing to the shortage of capital when German industry was developing, the banks were forced to make advances to industrial firms for capital expenditure, not only, as in England, for working capital. Such advances could not be as liquid as English banking tradition requires bank investments to be kept, and to protect them banks insisted on representation on boards of directors and took a continuous and active part in the direction of industry. The German banks, therefore, were intimately associated with industry, and were able to act as co-ordinating and mediating agencies when it was necessary to bring together a number of firms in which any bank was interested. They could go further and compel the formation either of a kartel or a merger, if they

judged it necessary. In order to exercise this power they equipped themselves with staffs of technical experts, who could both advise them and assist the firms they were interested in. When they had assisted a firm to expand, or a group of firms to combine, they did not at once disinterest themselves, but continued to nurse and develop their protégé.

English banking tradition is against such active intervention by the banks in industry. There is no doubt that it is a sounder tradition from the point of view of deposit banking, as was becoming recognised in Germany before the war. But the function of supplying the needs of industry for fixed capital, of associating with capital investment the service of technical experts, and of promoting the co-ordinated development of large-scale industry, is a function which remains for some agency to perform, even if the banks are not fitted to undertake it. After the collapse of prices in 1920, the English banks in many districts found themselves with large advances tied up in firms in depressed industries, which have never been able to repay them. Where the banks still have advances tied up, or hold debentures issued as security for such advances, they are just as much implicated in the conduct of industry as the German banks, and differ only in having never faced systematically the responsibilities of the position into which they have slipped, the position of controlling partners in industry, and used their power to compel a reorganisation of the industry.

In America there was a similar shortage of capital when modern industry was developing; but the need was met, not as in Germany by utilising the banks, but by the development of large dealers in capital—the merchant-bankers or issuing houses. These great firms

collected capital and put it at the disposal of expanding industry. They came thus to have the same relation to industry as the German banks. When any reorganisation was needed, there was an agency available that could co-ordinate and coerce industry into complying, and find any new capital that was needed to make the reorganisation effective.

London has merchant-bankers whose prestige is as great as that of any American house, and whose operations are on a comparable scale. But it is not the least of the handicaps under which British industry labours that these great houses, and the English capital market as a whole, are less interested in British manufacturing and mining industry than in other outlets for their activity. The whole historical development of English economic life has gone to produce this schism. Industries were established and developed by industrial capitalists in the provinces, and grew out of their own profits. Lancashire and the West Riding of Yorkshire never went to London for capital before the war, and many heads of North-country firms would not know where to apply in London if they did want additional capital. The leading London financial houses, on the other hand, grew by financing commerce, especially foreign commerce; from dealing in goods they came to deal in bills, and from creating bills they went on to issue and underwrite securities. The result is that London knows more perhaps of South America and China than it does of Bury or Bradford. It can judge to a nicety the credit-worthiness of a Balkan Government, a South American railway or an African mine, while it would hesitate to form a judgment on an English industry that provided a livelihood for as many people as the Balkan Government provided with law and

order. The South African gold-mining industry is organised by London financial houses, which supply it with experts in every aspect of its operation, finance for its development, and control for its co-ordination; but no similar service has been given by a London firm to the English coal-mining industry. London is consequently the easiest place in the world to raise capital for developing Central American municipalities, Australian irrigation schemes, Rhodesian copper mines, South American ranches and Malayan rubber plantations, because it has studied and understands the potentialities of the rest of the world. It has not given the same study to the potentialities and needs of Lancashire and Yorkshire. The gulf between London and England is no doubt being bridged. The banks are such a bridge, with their interests spread throughout the country. Investment trusts may find themselves forced to take a more active part in the reorganisation of British industry, and its control after reorganisation, in defence of the interests they have acquired in it and may acquire in the future. The newer industries have been financed from London to a greater extent than the old. There is more exchange of personnel than there was in the nineteenth century. But on the whole the London capital market still looks outwards, and has been of little assistance so far to the depressed industries in meeting the new situation with which they have been confronted since the war. Perhaps a change is taking place.

VII. *A Failure of Private Enterprise?*

Socialist and Labour critics are fond of referring to the post-war depression and unemployment as proof of

the failure of private enterprise. It would be as reasonable to refer to it as proof of the failure of Government, since it was caused by the war and the war was the work of Governments. In a sense, nevertheless, it is a failure of private enterprise, since the essential service of private enterprise is the spontaneous adaptation of industry to new opportunities and changed conditions, and adaptation to the changed conditions of the post-war world has still to be made. Moreover, the function of the issuing-house—the criticism of economic projects and the direction of the flow of capital to those that will justify capital investment by their return—is the most elementary and fundamental exercise of private enterprise. The reorganisation of the depressed industries calls for the exercise of just this function. It is, as we saw, a technical piece of work, which the heads of the firms in the industries are not themselves trained to perform, even if an outside agent and mediator could be dispensed with. It is, therefore, a failure of private enterprise at a crucial point—or at any rate the indication of a defect in the country's economic organisation—that the London capital market has not done more to study the needs and possibilities of the depressed areas. The Bank of England has interested itself and used its influence to promote reorganisation in certain cases; but the Bank has other not less important functions that it cannot delegate, and it might reasonably expect to be relieved of the task of reorganising British industry.

Private enterprise would appear to have "failed" from another point of view. The accumulation of capital should quicken industry and secure either the employment of more workers, or the employment of an unchanged number at higher wage-rates corresponding

with an increased productivity of industry. In England there is evidence of a steady accumulation of capital, not, it is true, at the pre-war rate, but at an annual rate very much in excess of the rate needed to employ the annual addition to the population of working age, without much impression being made upon the mass of unemployment. In Germany, and to greater or less degree in all other continental countries except France, the great obstacle to industrial expansion is a shortage of liquid funds; in England there is no such shortage, without the accumulation having any apparent effect upon the employment situation. At the beginning of 1929 the aggregate deposits of the London clearing banks are at practically the same level as at the end of the 1920 boom, and, owing to the fall in prices, they have over sixty per cent more purchasing power; yet industry is not able to make use of these facilities. A marked growth of deposits might have been expected to raise prices, but prices have tended downwards, while aggregate deposits have risen; the explanation may be either that the deposits are not turned over so frequently as at a higher price level—their velocity has declined—as Mr. M'Kenna suggested; or that the additional purchasing power is absorbed and retained in sustaining a rising price level of stock exchange securities instead of a rising price level of commodities. On the former hypothesis, private enterprise must be adjudged incapable of making at any rate the full potential use of the resources at its disposal; on the latter, to have put them to a use that increases neither national wealth nor employment.

It is not suggested that London is taking no interest in the capitalisation of British industry. The increase in public issues on home account—to 75 per

cent above the pre-war amount, after allowing for the change in the value of money, out of diminished savings—would refute such a suggestion. But these issues represent rather the active seeking out of profitable individual concerns for re-sale at a profit to the public, and the financing of new and speculative enterprises that appeal to the new post-war investing public, than any considered and scientific attempt to adapt the capital structure of the established industries of the country to the changed conditions of the post-war world. Yet in the existing economic organisation, if there is any provision at all for the performance of this fundamental and essential function, it is the issuing house. If the issuing houses do not undertake it, private enterprise provides no other organ.

VIII. *The Alternative—Government Enterprise*

In default of private enterprise there is a case for public enterprise. If what is lacking in industry to-day is the impulse and assistance to reorganisation, re-equipment, and revival that the enterprise of individuals and the flow of private capital have given to industry in the past, there is a case, on any theory of the relations of Government and industry, for an attempt by Government action to give impulse and stimulus. The object to be aimed at is not merely to supplement the activity for which private enterprise is responsible by temporary employment on public works, but to restore the conditions of profitable activity on the part of depressed private industry. The method to be explored is the possibility of directing more of the accumulating and accumulated capital savings of the country to the neglected industries, for

the purpose of reorganising and re-equipping them. Since no substitute for the employment which these have provided in the past offers itself, and no vitalising flow of capital to them is being directed to them by private agencies, some public agency is required.

The need of some such change in the relation of Government to industry in the abnormal conditions of the post-war depression has been recognised by the Trade Facilities Act.[1] The machinery of these Acts has been used to guarantee capital borrowings by individual firms to extend this equipment or to finance large contracts. While these guarantees have been considerable in relation to the needs and other resources of the firms applying for them, they have been trivial in comparison with the needs and other resources of industry as a whole. They have been given only on application from the firms requiring them, which has limited them to the small minority of firms in a position and with the will to expand; no attempt has been made to use the machinery to assist firms that wish merely to consolidate, without extending, an insecure business, no conditions imposed that necessary reorganisation should be effected. If it is legitimate to provide funds at the Government's risk for equipment, it is legitimate to provide funds for reorganisation. The task of forming a judgment on the purposes of a loan and the risks involved is much more difficult; but in principle there is no important difference. If, therefore, there are other groups of firms in the position of the Oldham spinners, burdened with debts the charges on which are steadily crushing them and preventing any unaided revival, capable of productive

[1] The most useful discussion of these is perhaps that contained in *The Third Winter of Unemployment*, by J. J. Astor and others.

economies provided that they combine and can get capital for a fresh start, a loan on the two conditions, that creditors reduce their claims (or at least give the Government loan priority) and that a combination offering a prospect of technical and commercial economies be formed, would be a reasonable and a modest contribution for Government to make to revival. The joint conference of trade union leaders and employers, organised by Lord Melchett, recommended such an extension of the use of Trade Facilities Acts, and the support of organised labour is a virtual promise of labour co-operation in the necessary reorganisation.

But it is not sufficient for the Government to wait for applications. As we have seen, there are almost insuperable obstacles to the spontaneous reorganisation of a depressed industry by the firms in it; and, when circumstances make it possible for these to be overcome, capital can usually be obtained without Government assistance. The great need is not the loan of capital—that is only the justification for intervention by a Government agency and the inducement to welcome it—but initiative, enterprise, the impulse to reorganise, the pressure to face the changed situation and adapt industry to it. These Government must supply, if the issuing houses and other agencies of the capital market do not supply them. Such a policy would involve the establishment of an organisation of the type of an issuing house. The Government would have to secure the services of men of the training and judgment needed to examine proposals for reorganisation and capital expenditure and to carry through the negotiations that would ensue. London has no dearth of such men. It would have to supply them with

staffs of accountants and technical experts, who could provide them with the material of an expert or technical character for their judgment; again London has the accountants, and existing Government Departments have the technical experts.

A commission, so equipped, empowered to offer a guaranteed loan when its conditions were accepted, could not only consider proposals emanating from firms or groups of firms in the depressed industries, but could take the initiative, review in turn the needs of the industries that appear to need reorganisation, and make proposals to them. It would be the executive counterpart of the Balfour Committee, just as the Poor Law Commission set up by the Poor Law Amendment Act was the executive counterpart of the Inquiry Commission that produced the 1834 Report. If no executive organ is created to approach in turn the industries and interests reviewed, and urge upon their attention the conclusions and recommendations reached, the Balfour Reports, though valuable to contemporary students of economics and future historians, will be entirely without practical effect. With the experience of all the committees and commissions that have inquired into the problems of industry since the Reconstruction Committee was set up in 1916, it is sufficiently obvious that British industry does not respond to a treatment of mere advice. In the same way, to take a rough parallel, the Department of Scientific and Industrial Research, armed with its million grant, approached the industries of the country and established co-operative research associations, which the industries would never have established for themselves. It could submit each to an examination, that would be not less expert or adequate for its immediate purpose

than that to which the Samuel Commission subjected the coal industry, but less public, and therefore less controversial. The less formal and more elastic its procedure, the further it could be kept away from the grandiose associations of "General Staffs" and "Committees for National Development and Employment", the nearer it could be brought to the type and methods of a London or New York issuing house or a German bank, the more effective it would be. Invalids, like the depressed industries, even when they are convalescent, dislike publicity, noise, and controversy, and their feelings, however unreasonable, must be respected, if a cure is to be effected.

What is suggested in the preceding paragraphs is no more than has been done by the State, with the support of every political party, for the electricity supply industry and the railway industry. It is no more than was done by the Ministry of Munitions in the war.[1] If any objection is raised to its legitimacy, as distinct from its feasibility, it is a sufficient answer that the war on its economic side cannot be said to be over until employment is normal once more. There would be risks, large risks, if the provision of capital were on the scale needed to carry through a re-equipment by British industry equal to that which French industry has received since 1918—a re-equipment that might be financed by reparations receipts, as French re-equipment was financed; but the risks are not greater than those involved in alternative proposals for relieving unemployment, and much less than the risk

[1] The Government's insistence on co-operative working during the war is illustrated by the story of certain cloth manufacturers, who protested against the terms of a contract negotiated by the War Office with the local federation of manufacturers. They were told that the Government could deal only with associations, not with individuals, whereupon they formed "The Huddersfield Association of non-Federated Manufacturers"!

of leaving the depressed industries to make the inevitable adjustment to post-war conditions by the harmful and uncontrolled process of individual bankruptcies.

Consider the alternative proposals. If the country spends £145 millions on roads, and another £55 millions on houses, telephones, and the other objects of the Liberal party's proposal, there will be a return; but obviously there is a risk that the return will not be equivalent to the expenditure; yet the existing unemployment justifies the taking of a risk. The risk of loss, if an equivalent sum were advanced, on conditions laid down in each case by an expert *ad hoc* executive commission, to the depressed export industries, is probably not greater, since these industries were established, and demonstrated their suitability to English conditions before the war, without subsidy, protection or other adventitious aid. Again, there is a risk of loss if British credit be pledged to finance development in the non-self-governing colonies; if the loans are given interest free, there is a certainty of direct loss; yet the indirect advantages to be anticipated may nevertheless justify the expenditure. Is there any reason to suppose that the economic development of Lancashire or Durham would be any more risky? Certainly the material for forming a sound business judgment is more ample in the latter case. There is no objection raised by any party to the expenditure of £50 millions in exporting and settling in the Dominions British citizens, who have cost not less than £500 apiece to educate and bring up to the age at which they can make some return for the cost of their upbringing; would it not be worth while making some estimate of the number of Englishmen who could be reabsorbed in the West Riding woollen industry or the North-East Coast steel industry by a

judicious expenditure of something less than £50 millions? It is significant that American capitalists do not show the same despair of the future of British industry, and are ready to buy British industrial securities on the basis of a 2 or 3 per cent yield and apply new capital to their development.

The proper objects of such expenditure would be revealed, if they are not already known, by the inquiries which the Government commission would conduct in its approach to the depressed industries. That there are objects which would justify expenditure is frequently indicated. Sir Richard Redmayne, who speaks on both the technical and economic aspects of coal-mining with unique authority, has not only shown in his evidence before the Sankey Commission the economies to be anticipated from concentration of the mining industry, but has indicated (in the correspondence columns of *The Times*) less ambitious programmes of technical re-equipment that would justify their cost, if the capital for them could be provided, even in the present depressed commercial condition of the industry. The £23 millions of the Coal Subsidy, had it been a conditional grant directed to improving the permanent competitive efficacy of the industry, would probably have covered all the improvements that current technique would suggest. The first report of the National Fuel and Power Commission (§61) has the following comment on a related and equally depressed industry: "We recognise the real financial difficulties of the coke-oven industry but at the same time we are left with the impression that the coke-oven plant of the country is in general far below the standard of efficiency that our needs require, and we recommend that the owners should, in many cases, consider plans for reorganising

their oven plants as soon as possible into installations serving a number of collieries and equipped with a modern type of oven. The question of the most suitable location for the plant also requires consideration."[1] The textile industries would also be benefited by some of the new and improved machinery which the British textile machinery manufacturers have exported in such large quantities to their competitors since the war.[2]

[1] The following comment on this paragraph was made by a very successful firm of engineers interested in colliery and coke-oven equipment to whom I showed it: "We have gone into this matter for one of the biggest steel works in the country and find that the cost of suitable [coke-oven] plant would be £350,000, and that after allowing interest at 5 per cent and depreciation at 7½ per cent (which is ample), there would be a profit of £58,000 per annum. Alternatively this would be equivalent to a reduction of nearly 3s. per ton on the coke produced or 7s. 6d. a ton on steel. The firm in question have, like most steel works, no surplus capital at all, and would (naturally) very much like a trade facilities grant to enable them to put in hand this work. I am satisfied that the figures can be taken as being on the safe side."

[2] Cf. the following extract from the Mather Lecture by the Secretary of the Department of Scientific and Industrial Research, before the Textile Institute on April 11th 1929. (*Journal of the Textile Institute*, No. 4.) "But would it not be true to say that in the textile industries we have a typical example of the inevitable sequence of events which occurs in every industry which sets itself out to produce an article in common demand by the processes of mass production? . . . All the machines used in the textile industries are out of date. None of them has really received the close scientific study and analysis which the provision of scientific instruments to-day permits to be carried out with the greatest accuracy. Like any other machine the design of which, on broad lines, dates back to the early part of the nineteenth century, they have been developed as a result of what might be called the flashes of inspiration of comparatively few men, and they fall short of practical perfection because their imperfections have never been subjected to close scrutiny. . . ."

"I can hear the textile industry move uneasily and inquire whether I am seriously suggesting that its equipment should be scrapped. I am, indeed, suggesting that all industries, and especially the textile industry at this moment, should be prepared to contemplate the scrapping of any machinery which has been, let us say, ten to twenty years in use. But I agree that the re-equipment of the textile industries is not easy to bring about just now, if only for the fact that the type of investigation I have in mind has not gone very far. In the chief textile research associations it has, however, gone far enough to indicate that the possibility of substantial improvement in standard equipment rests on more tangible evidence than the dreams of an arm-chair critic."

The only comment that is necessary is that in the cotton and wool textile industries there is very little machinery which has *not* "been ten to twenty years in use".

The objection to putting State credit on a large scale at the disposal of the depressed industries is not, then, that risk of loss would be involved. Equally incalculable risks are equally involved in doing anything else or in doing nothing. The objections that may be raised are that it is not feasible to secure by any State action the appropriate application of the capital, and that it is not legitimate to give public assistance of this sort to industries working for private profit. The first of these objections cannot be pressed. It is feasible, if the administration of the Trade Facilities Acts was feasible, since that involved the same problems of judgment and discrimination. It is feasible, if safeguarding is feasible, since this also involves discrimination between applicants and consideration of the needs of an industry as a whole. It is feasible, if it would be feasible when undertaken by an issuing house or syndicate of issuing houses, as it would be in America; for the Government could copy the organisation and methods of issuing houses. Doubtless it would be better done by private issuing houses, so that a Government authority had not the ungrateful task of discriminating between applicants and imposing unpleasant conditions of reorganisation; but, in fact, it is not being done, at any rate on an adequate scale and at an adequate rate, by private issuing houses. It is still possible for the capital market to make Government action unnecessary by taking the initiative itself.

The objection to public grants in aid of private enterprise, though politically more likely to receive attention, has even less substance. Private industry is not private in the sense that it is not a matter of public concern. It is private only in the sense that, as a matter of convenience and expediency, it is left to be

administered, under conditions laid down by public regulation, by individuals working for wages, salaries, and profits. Profits are a condition of its successful operation; that is a statement of fact. It may be argued that this system should be changed, and industries subjected to a more conscious and deliberate public direction; but until that change is made, the conditions of the present system must be observed, and to leave large parts of industry without the power of making profits is to condemn them, and the workpeople who depend on them, to depression and unemployment. Even if a change of system is desirable, it may be doubted whether the abnormal conditions of the post-war world offer a favourable opportunity; although the present owners of the mines, the railways, and many firms in all the export industries would doubtless gladly exchange their property for Government securities if they were offered anything like the cost of their investment for it. While the present system of control is maintained, however, there is no objection on grounds of public principle to assisting the depressed industries by public grants. Even if private proprietors and shareholders benefit thereby, their benefit is a condition and the means whereby their employees and the country as a whole is benefited. At the outset of this inquiry we discovered that the central regulator of industrial activity was the *entrepreneur's* fluctuating margin of profit; if we grudge the restoration of a positive margin, we cannot expect industrial recovery. The American wage-earner since 1920 has not been worse off than his English fellow-worker, merely because the American employer has made larger profits than the English employer.

General considerations like these do not exhaust the

case for special Government assistance to the depressed industries. As we have seen, their plight is very largely due to abnormal expansion stimulated by the war, so that the cost of relieving it should in equity be treated as a war cost, to be borne by the general taxpayer. And all the significant acts of public policy since the war have added to the burden. The peace treaties set up new states, which added 20,000 miles to the tariff boundaries of Europe; the prosperous building, gas, road-transport, and other sheltered industries suffered no detriment from this, but the export industries found their trade dislocated and their markets lost. The reparations settlement, which encouraged German deliveries in kind, dislocated the trade of the British coal and steel export industries. Reparations also financed the reconstruction of French and Belgian industries, to compete with English industries that had not been reconstructed. The reduction in armaments deprived an important part of the British engineering and shipbuilding industries of their accustomed outlet, and so destroyed the value of a large part of their fixed capital. By driving them into other fields, it undermined the prosperity of commercial shipbuilding and engineering. It is not suggested that these unfortunate economic reactions upon English industries are reasons for adopting different policies; but they are reasons for special consideration of the industries incidentally affected.

All these influences together are of less importance than the return to the Gold Standard. It must be insisted that the return was necessary. No practical alternative to the Gold Standard, whether as a device for stabilising prices, or for restoring the pre-war stability in the exchanges, and consequently in foreign

trading, or for protecting Central Banks against interference by Governments, offered itself. And, if the restoration involved losses for one set of interests, it was essential to others as important. The business of London as an international money market depended on it; the large income derived from foreign investments, on which fixed interest is paid in sterling, required it; the country's dependence on imported food and raw material required it. But the very reduction in prices and raising of sterling exchange rates, which benefited these interests, imposed an intolerable handicap on the export industries. To be fair to them, the restoration called for a reduction in wage rates, in interest charges, in charges for social services; but post-war legislation, by extending legalised collective bargaining and giving it the support of a national system of unemployment relief, has made the English wage-system the most inelastic in the world. Bondholders are under no legal obligation to refrain from exacting their bond; charges for social services and local rates (until the present year) have been steadily increased. The inevitable and, from the point of view of the country as a whole, justified social costs of restoring the Gold Standard after the currency abnormalities of the war have been concentrated upon the export industries. If their claim in equity to special consideration be ignored, the country excusing itself by unsustained allegations of "inefficiency", an effort to restore them would be justified on the merest grounds of expediency.

The assumption so far has been made that the Government can give all the assistance to the depressed industries that is likely to be effective by initiating reorganisation and proffering financial assistance. But the possibility that compulsion may be needed should

not be ruled out. The precedent of the compulsory reorganisation of the railways under the 1921 Act is there, if the only alternative is to continue indefinitely subsidising unemployment by a tax on employment. The objections to compulsion are not objections of principle, but difficulties of application. Although the causes of post-war depression are different from the causes of pre-war depression, the condition of recovery is the same—the restoration of a positive margin between costs and selling prices. If by State action we have brought selling prices down, and by State action we are keeping costs up, we may be forced by State action to compel a reorganisation of the industries that cannot in their present form meet these handicaps.

The issue will arise in a concrete form at the end of the present year. The restoration of prosperity to coal-mining is the first condition of any general recovery. Its size and importance among the depressed industries, its basic relation to other industries, its function in supplying the only bulk export to balance the bulk imports by British shipping, give it priority in any solution of the unemployment problem. The wage agreements in the principal districts,[1] imposed upon the miners after their defeat in the 1926 coal-mining dispute, run out at the end of the year. The situation with which the industry was faced at the end of 1920 and at the end of 1925 will recur. The mine-owners will argue, with justification, on their tacit assumption that no reorganisation is to be attempted, that the industry cannot afford to pay higher rates of wages, and may even claim a reduction, which

[1] Scotland, Yorkshire, South Wales, Lancashire and Cheshire, and Cumberland. In addition, the agreements in Durham and Northumberland can be terminated at short notice.

the commercial returns of every district up to the last quarter of 1928 would justify. The miners, who accepted the reductions of 1926 under compulsion and not from conviction of their necessity, and whose earnings bear a lower ratio to pre-war earnings than those of any other important class of workers except the iron and steel workers, will argue that they are entitled to an advance, and will certainly resist a reduction. They will claim that, if the industry cannot as at present organised pay higher rates, it could be made to pay higher rates by methods of reorganisation which are well known and which the mine-owners might have applied. They will cite the reports of the Sankey and Samuel Commissions, point to the example of the German coal industry (not that it has been able to escape the results of world over-production) and the English chemical industry; refer to the witness of the Balfour Report, the Liberal Industrial Inquiry, the Mond Conferences, and private investigators, as to the possibilities of rationalisation—all of which, if the precedents of 1921 and 1926 can be trusted, will leave the mine-owners unmoved. The issue was "settled" in 1921 by a lock-out, which exaggerated the effects and delayed recovery after the initial slump; it was "settled" again in 1926 by a lock-out, which exaggerated the check to activity and delayed recovery after the final return to the Gold Standard. Whatever Government is in power when the issue arises, if the industry has no alternative to offer except a third "settlement" of this expensive character, it is hard to believe that some compulsion to reorganise will not be applied.

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THE END

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